THE FEDERAL BAILOUT OF AIG

HEARING

BEFORE THE

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

SECOND SESSION

JANUARY 27, 2010

Serial No. 111–107

Printed for the use of the Committee on Oversight and Government Reform

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U.S. GOVERNMENT PRINTING OFFICE

63–136 PDF WASHINGTON : 2011

For sale by the Superintendent of Documents, U.S. Government Printing Office
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THE FEDERAL BAILOUT OF AIG

WEDNESDAY, JANUARY 27, 2010

HOUSE OF REPRESENTATIVES,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, DC.

The committee met, pursuant to notice, at 10:10 a.m., in room 2154, Rayburn House Office Building, Hon. Edolphus Towns (chairman of the committee) presiding.

Present: Representatives Towns, Kanjorski, Maloney, Cummings, Kucinich, Tierney, Clay, Watson, Lynch, Cooper, Connolly, Quigley, Kaptur, Norton, Davis, Van Hollen, Cuellar, Welch, Foster, Driehaus, Chu, Issa, Burton, Mica, Duncan, Turner, Westmoreland, McHenry, Bilbray, Jordan, Flake, Fortenberry, Chaffetz, Schock, Luetkemeyer, and Cao.

Also present: Representatives Blunt, Bachus, and Stearns.

Staff present: John Arlington, chief counsel—investigations; Beverly Britton Fraser, counsel; Lisa Cody, investigator; Brian Eiler and Neema Guliani, investigative counsels; Adam Hodge, deputy press secretary; Carla Hultberg, chief clerk; Marc Johnson and Ophelia Rivas, assistant clerks; Phyllis Love, Ryshelle McCadney, Christopher Sanders, and Alex Wolf, professional staff members; Mike McCarthy, deputy staff director; Amy Miller and Gerri Willis, special assistants; Leah Perry and Steven Rangel, senior counsels; Jason Powell, counsel and special policy advisor; Jenny Rosenberg, director of communications; Joanne Sanders and Christopher Staszak, senior investigative counsels; Leneal Scott, IT specialist; Shrita Sterlin, deputy director of communications; Ron Stroman, staff director; Lawrence Brady, minority staff director; John Cuaderes, minority deputy staff director; Rob Borden, minority general counsel; Jennifer Safavian, minority chief counsel for oversight and investigations; Frederick Hill, minority director of communications; Adam Fromm, minority chief clerk and Member liaison; Kurt Bardella, minority press secretary; Seamus Kraft and Benjamin Cole, minority deputy press secretaries; Tom Alexander and Christopher Hixon, minority senior counsels; Daniel Epstein, Chapin Fay, Hudson Hollister, and Mitchell Kominsky, minority counsels; Brien Beattie, Molly Boyl, Alex Cooper, Meredith Liberty, and Mark Marin, minority professional staff members; Sharon Casey, minority executive assistant; Stephanie Franco, minority press secretary and communications liaison; Ashley Swope and Mike Whatley, minority staff assistants.

Chairman TOWNS. The committee will come to order.

Good morning.

On September 16, 2008, the Wall Street giant AIG faced immediate bankruptcy. AIG was saved from collapse when the American people came to the rescue with an $85 billion bailout. Less than 2 months later, the American taxpayer was again forced to pay the bill when the Federal Reserve directed AIG to hand out billions of dollars to counterparties that included the biggest names on Wall Street.

In effect, the taxpayers were propping up the hollow shell of AIG by stuffing it with money, and the rest of Wall Street came by and looted the corpse.

The circumstances surrounding the payments to the counterparties has created an air of suspicion and distrust among the American people, starting with the New York Fed's initial refusal to name the counterparties.

The New York Fed argued that disclosing these counterparties would somehow injure AIG. In fact, when the information was finally released under pressure from Congress, nothing happened. It had absolutely no effect on AIG's business or financial condition.

But it did have an effect on the credibility of the Federal Reserve and it called into question the Fed's penchant for secrecy. We need to change the culture on Wall Street and the culture among the regulators, from secrecy to transparency, recognizing that only truly confidential competitive or consumer information should be protected.

As we sit here a year and a half later, after AIG handed out billions in taxpayer dollars, because of this secrecy, we still don't know why or how the decision to rescue AIG was made, or who made the decision to offer AIG's trading partners 100 cents on the dollar in the so-called counterparty payments.

Every day in the business world, when a company is having financial problems, its creditors have to take less money than they are owed. Otherwise, they risk not getting any money at all.

They call this a "haircut." In the case of AIG, nobody got a haircut. Instead, they were given a piggy bank full of taxpayer dollars and said help yourself. Let me just say plainly that I think just about every American would say the government should have forced AIG's counterparties to take less money.

Evidently, major decisions were made by a combination of the Federal Reserve, the Federal Reserve Bank of New York, and the Bush Treasury Department. Today, we will hear from witnesses who were involved in making these decisions, and we hope they can shed light on a murky set of facts.

Under subpoena, the committee obtained more than 250,000 pages of documents from the New York Fed detailing its handling of the AIG counterparties. Particularly disturbing is the fact that these emails indicate that AIG proposed to disclose to the SEC and the public the names of the counterparties and the payments. But it was the New York Fed that directed AIG to withhold this information. As one New York Fed staffer put it, "any public disclosure by AIG is still subject to Fed approval."

At least two things are clear here: The entire financial regulatory system was broken, and there shouldn't be any more bailouts. The lack of transparency we have seen in the double bailout of AIG leads to distrust, which leads to anger.

The question that looms over all of this: How do we prevent a repeat of this financial crisis in the future? Unless the Congress adopts genuine financial services reform, it will be only a matter of time before we see another AIG, another Bear Stearns, another Lehman Brothers, and the next big bank will be "too big to fail" and the taxpayers will wind up footing the bill again and again and again.

I ask my Republican colleagues on this committee to join with me in fixing the system. Blame is about yesterday. Fixing the system is about today and the future.

In the AIG case, we can talk all we want to about complicated business deals, but this all boils down to a simple concept: when average people were losing their homes and jobs, the same big banks that caused the problems got every dollar back, courtesy of the American taxpayer. And the Federal Reserve tried to keep important information a secret.

Secrecy leads to distrust. And the American people now distrust what happened in these bailouts. Congress has the right to know how and why that happened and the American people have the right to know how and why that happened.

I hope that today we can get answers to these and other important questions.

[The prepared statement of Chairman Edolphus Towns follows:]

OPENING STATEMENT OF CHAIRMAN EDOLPHUS TOWNS

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

January 27, 2010

"The Federal Bailout of A.I.G."

Good Morning.

On September 16, 2008, the Wall Street giant AIG faced immediate bankruptcy. AIG was saved from collapse when the American people came to the rescue with an $85 billion bailout. Less than two months later, the American taxpayer was again forced to pay the bill when the Federal Reserve directed AIG to hand out billions of dollars to counterparties that included the biggest names on Wall Street.

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I ask my Republican colleagues on this Committee to join with me in fixing the system. Blame is about yesterday. Fixing the system is about the future.

In the AIG case, we can talk all we want about complicated business deals, but this all boils down to a simple concept – when average people were losing their homes and jobs, the same big banks that caused the problems got every dollar back, courtesy of the American taxpayer. And the Federal Reserve tried to keep important information secret.

Secrecy leads to distrust. And the American people now distrust what happened in these bailouts. Congress has the right to know how and why that happened and the American people have the right to know how and why that happened.

I hope that today we can get answers to these and other very important questions.

Chairman TOWNS. I now yield to our ranking member, the gentleman from California, Congressman Darrell Issa for his opening statement.

Mr. ISSA. Thank you, Mr. Chairman. You have our promise that this has been and will continue to be a bipartisan oversight of these and all the issues related to the Fed's current and future authority.

Mr. Chairman, I would like to ask unanimous consent, pursuant to our rules, that Spencer Bachus, the ranking member on Financial Services Committee; Kevin Brady of Texas, the ranking House Republican on the Joint Economic Committee; Roy Blunt, the former Whip; Ron Paul, whose credentials on this are well understood; and Cliff Stearns of Florida be allowed to sit on the dais and, should there be time, allowed to ask questions pursuant to the rules.

Chairman TOWNS. Without objection.

Mr. ISSA. Additionally, I would ask, at this time, to submit for the record Schedule A, which is in fact the shortfall agreements between Maiden Lane III and AIG Financial Products, since they will be referred to in questioning, and we want to make sure they are officially in the record.

Chairman TOWNS. Reserving the right to object.

Mr. ISSA. OK.

[The information referred to follows:]

List of Derivative Transactions

Schedule A
to
Shortfall Agreement

CUSIP / ISIN of Underlying CDO Issue Assets Included in 11/25/2008 Closing	Counterparty	Tranche Name	Notional Value	Total Collateral Posted	Negative Mark to Market
[Redacted]	SOCGEN	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	SOCGEN	[Redacted]	[Redacted]	[Redacted]	[Redacted]
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[Redacted]	GSCM	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	GSI	[Redacted]	[Redacted]	[Redacted]	[Redacted]

List of Derivative Transactions

Schedule A
to
Shortfall Agreement

CUSIP / ISIN of Underlying CDO Issue	Counterparty	Tranche Name	Notional Value	Total Collateral Posted	Negative Mark to Market
[Redacted]	GSI	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	GSI	[Redacted]	[Redacted]	[Redacted]	[Redacted]
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[Redacted]	GSI	[Redacted]	[Redacted]	[Redacted]	[Redacted]
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List of Derivative Transactions

Schedule A
to
Shortfall Agreement

CUSIP / ISIN of Underlying CDO Issue	Counterparty	Tranche Name	Notional Value	Total Collateral Posted	Negative Mark to Market
[Redacted]	ML	[Redacted]	[Redacted]	[Redacted]	[Redacted]
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[Redacted]	BGI	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BOA	[Redacted]	[Redacted]	[Redacted]	[Redacted]
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[Redacted]	CORAL Purchasing (Ireland) 2 Limited	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	DB	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	REMO FINANCE INC - Dresdner	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	UBS	[Redacted]	[Redacted]	[Redacted]	[Redacted]
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[Redacted]	UBS	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	UBS	[Redacted]	[Redacted]	[Redacted]	[Redacted]

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[Redacted]	UBS	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BARCLAYS	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BARCLAYS	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BARCLAYS	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BMO	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BMO	[Redacted]	[Redacted]	[Redacted]	[Redacted]
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[Redacted]	BMO	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BMO	[Redacted]	[Redacted]	[Redacted]	[Redacted]
[Redacted]	BMO	[Redacted]	[Redacted]	[Redacted]	[Redacted]
		Totals - Assets Included 11/25/2008 Closing	**$46,119,130,493**	**$25,854,602,616**	**$25,060,896,305**

Mr. ISSA. Additionally, Mr. Chairman, I would ask unanimous consent that the eight letters previously sent to Secretary Geithner and, as of today, not responded to also be placed in the record at this time, although they will not be reviewed further during this hearing.

Chairman TOWNS. Reserving the right to object.

Mr. ISSA. Thank you, Mr. Chairman.

Thank you, Mr. Chairman, for all of this and more. Working together with you on the subpoena documents has caused both the majority and minority to glean considerable new information.

In recent weeks, this committee, receiving these documents have caused us to better understand the New York Fed pressured AIG to abort negotiations designed to obtain a haircut, as it was called, from its counterparties and keep the details of the counterparties' payments from appearing on the firm's forms at the SEC.

Today, one of the questions we will ask is should the American people be kept from knowing until 2018 the details of who were the ultimate beneficiaries of this bailout.

As I have said before, I consider this a back door bailout. The people giving us testimony today will tell us that they felt that this was essential and necessary. Mr. Chairman, as you can recall, AIG's founder, Hank Greenberg, has previously testified, along with AIG CEO Edward Liddy. And in that testimony Hank Greenberg made it very clear that he believed that: one, hedging should have occurred sooner; and, two, bankruptcy would have been a cleaner way to resolve a company in which he is the largest stockholder.

I am proud to say, after that hearing, AIG has re-engaged their founder to help them maximize the value of a company that is currently 80 percent owned by the American people.

Not to say that there is a lot of good news at AIG. Mr. Chairman, it is clear that the money paid and it being kept secret may ultimately cause the American people never to be repaid these dollars.

Can you hear me OK now? You can't? OK. Now. OK, I will focus on this mic this time. Usually the problem is I am too well heard, right, Mr. Chairman?

Chairman TOWNS. Generally.

Mr. ISSA. Today we will have an opportunity to ask questions and the American people will have the right and I believe will receive straightforward answers.

So far, Mr. Chairman, this is what we know. We know that some of today's witnesses played a central role in the decision to bail out AIG, rather than allow the normal bankruptcy procedures to run their course. We know that one of today's witnesses made the decision to pay AIG counterparties at 100 cents on the dollar. We know that one of today's witnesses was the primary architect of the AIG Trust Agreement, whereby the taxpayers' investment in AIG is managed not in the interest of the U.S. taxpayers, but of the U.S. Treasury Department. That was from previous testimony and we rely on that to say perhaps that is not the right answer.

We know that the New York Fed sought to cover the counterparty payments made possible by the taxpayers' money. We now better understand that the New York Fed transferred their earlier responsibility to the American people after TARP was passed. We know that the New York Fed succeeded in getting the SEC to continue the cover-up until 2018, 10 years from the date the bailout began. And we know that the full amount paid to AIG's counterparties will likely never be repaid to the American people.

Some facts, Mr. Chairman, remain unknown or uncertain. Secretary Geithner has claimed publicly that he recused himself from the day-to-day management of the New York Fed when the cover-up occurred. In fact, he has asserted complete ignorance of the Fed's efforts to cover up the bailout details. Many people, including members of this committee, have a hard time believing that Secretary Geithner entered into an absolute cone of silence—for those of us old enough to remember what that was—on the day his nomination was announced. Where was Secretary Geithner for the months and months that back door bailouts were being questioned in the media? Did he ever wonder why his decision to pay AIG's counterparties was kept secret for so long?

These are the questions the American people deserve.

Mr. Chairman, I would ask unanimous consent the remainder of my opening statement be placed in the record at this time.

Chairman TOWNS. Without objection, so ordered.

Mr. ISSA. Thank you, Mr. Chairman. I yield back.

[The prepared statement of Hon. Darrell E. Issa follows:]

EDOLPHUS TOWNS, NEW YORK
CHAIRMAN

DARRELL E. ISSA, CALIFORNIA
RANKING MINORITY MEMBER

ONE HUNDRED ELEVENTH CONGRESS

Congress of the United States

House of Representatives

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

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Statement of Rep. Darrell Issa, Ranking Member

"The Federal Bailout of AIG"

January 27, 2010

Thank you, Mr. Chairman, for holding today's hearing on the government's efforts to hide the full truth from the American people about the way their tax dollars were spent in the bailout of AIG.

In recent weeks, this Committee received a series of documents that revealed the degree to which the New York Fed pressured AIG to abort negotiations designed to obtain a haircut from its counterparties and keep the details of counterparty payments from appearing in the firm's SEC filings. More documents – received last week under subpoena from this Committee – have added to the picture of what really happened in the government bailout of AIG.

In the course of our investigation, Mr. Chairman, this committee has heard from AIG's founder, Hank Greenberg, and former AIG CEO, Edward Liddy. We have heard from the three members of the AIG trust, a tragically-flawed entity designed by today's witness, Secretary Geithner, while he was still President of the New York Fed.

With each hearing, and with each passing month since the decision was made to bail out AIG with more than $180 billion of taxpayer money, more questions have arisen about the way decisions were made, who made those decisions, who knew about them, and who wanted them kept secret.

Today, we have the opportunity to ask these questions, and the American people have a right to straightforward answers.

So far, Mr. Chairman, this is what we know:

We know that some of today's witnesses played a central role in the decision to bail out AIG rather than allow normal bankruptcy procedures to run their course.

We know that one of today's witnesses made the decision to pay AIG's counterparties at 100 cents on the dollar.

We know that one of today's witnesses was the primary architect of the AIG trust agreement whereby the taxpayer investment in AIG is managed ***not*** in the interest of the U.S. taxpayers but of the United States Treasury Department.

We know that the New York Fed fought to cover up the counterparty payments made possible by taxpayer money.

We know that the New York Fed succeeding in getting the SEC to continue the cover up until the year 2018, ten years from when the bailout began.

And we know that the full amount paid to AIG's counterparties will likely never be repaid to the American people.

Some facts, Mr. Chairman, remain unknown or uncertain. Secretary Geithner has claimed publicly that he had recused himself from day-to-day management of the New York Fed when the cover-up occurred. In fact, he has asserted complete ignorance of the Fed's efforts to cover up the bailout details.

Many Americans, including members of this Committee, have a hard time believing that Secretary Geithner entered an absolute cone of silence on the day that his nomination was announced. Where was Secretary Geithner for the months and months that the backdoor bailouts were being questioned in the media? Did he ever wonder why his decision to pay AIG's counterparties was kept secret for so long?

These questions deserve answers.

At the height of the AIG bailout, the argument was made that a cover up of AIG's counterparty payouts was necessary to protect U.S. taxpayers from a deeper economic recession. In order to protect the American people from themselves – the argument goes – the New York Fed had to keep them in the dark. Fed officials have since acknowledged that these doomsday predictions about disclosure were overstated.

A similar chain of deception occurred when Members of Congress were given another ultimatum: pass a mass bailout to purchase toxic mortgage-backed securities or the international economy will collapse. This was presented as the only option to save the global financial system. The fallacy of this "only option" was exposed when officials, after getting legislation passed through Congress, quickly pivoted and decided instead to use TARP for direct capital injections into large financial institutions.

Indeed, the change in TARP strategy may very well have been fueled by problems that government officials encountered in the AIG bailout. This may have forced Federal officials to rethink their plan to buy and manage toxic assets. This committee needs to investigate the change in TARP strategy, whether or not alternatives to the AIG bailout were ever seriously discussed, and the connection between the AIG bailout and the TARP bailout.
It remains a mystery, after all these lessons and course changes, why the Federal Reserve insists on keeping key details on the backdoor bailout of AIG's counterparties secret until 2018. The cover-up continues.

Despite these missteps, I believe that Secretary Geithner, in fact, is sincere in his efforts to rebuild the American economy. I also believe that Secretary Geithner sincerely wants to see Americans go back to work, see their retirement portfolios returned to profitability, and see their lives put back together.

I believe, however, that these aspirations – aspirations that we all share, I might add – will never be realized so long as this Congress and this Administration continue to pursue a reckless course of more bailouts and bogus stimulus programs instead of allowing the private sector to create new business opportunities and the jobs that come with them.

Today, and in the days of ongoing investigation that will follow today's hearing, the American people will have a chance to hear Secretary Geithner's answers and explanations, as well as those of other government witnesses. And they will have a chance to determine whether the pattern of secrecy, cover-ups, and greater federal control and more government bailouts is the way to resolve our economic problems.

I have looked forward to this important hearing for months, and I look forward to hearing from today's witnesses. I thank you, Mr. Chairman, for the way you have worked with me to see this hearing come to pass.

Chairman TOWNS. I thank the gentleman from California.

At this time we would like to turn to our first witness, Treasury Secretary Geithner.

It is committee policy that all witnesses are sworn in, so, Mr. Secretary, if you would stand and raise your right hand.

[Witness sworn.]

Chairman TOWNS. Let the record reflect that he answered in the affirmative.

You may be seated.

STATEMENT OF TIMOTHY F. GEITHNER, SECRETARY, U.S. DEPARTMENT OF THE TREASURY

Secretary GEITHNER. Chairman Towns, Ranking Member Issa, members of the committee, thank you for the opportunity to testify before you today. I welcome the committee's attention to this issue, and we will continue to work closely with this committee, with all other oversight bodies——

Chairman TOWNS. Mr. Secretary, pull the mic just a little closer. We are having a little trouble.

Secretary GEITHNER. I am almost eating it.

Chairman TOWNS. I know.

Secretary GEITHNER. How does that sound?

Chairman TOWNS. Shows you how our sound system is not too good around here. We keep making budget cuts.

Secretary GEITHNER. I don't think I can make it any closer.

I want to make sure that the American people have a comprehensive view of the actions we took to end this financial crisis.

Deciding to support AIG was one of the most difficult choices I have ever been involved in in over 20 years of public service. The steps that were taken were motivated solely by what we believed to be in the public interest. We did not act because AIG asked for help. We did not act to protect individual institutions. We acted because the consequences of AIG failing would have been catastrophic for our economy and for American families and businesses.

More than a year removed from that terrible week of September 2008, I believe that the Government's strategy—and it was the Government's strategy—was the best of the available options and will ultimately cost the taxpayer far less than many feared and far less than many alternatives many people suggest today would have been better. And, importantly, if you join with the President in adopting his proposed financial responsibility fee, American taxpayers will not have to pay one cent for the actions we took in AIG or the actions we took with the authority Congress gave the administration to stabilize this financial crisis.

AIG's problems became acute just a few days before Lehman declared bankruptcy. At that time, our financial system and our economy stood at the brink of collapse. The banks and financial institutions that Americans rely on to protect their savings, to help finance their children's education, to help pay their bills were risks which few Americans had ever experienced. The banks and the financial markets that businesses rely on to meet payroll, to build inventory, to fund new investments, to create new jobs were threatened like at no time since the Great Depression. Across the country, across the United States of America, people were rapidly losing confidence in our financial system and in the Government's ability to safeguard their economic security.

In the midst of this storm, AIG posed a much greater threat than Lehman. AIG was much larger; it was spread across the globe; and its failure would have been far worse, hitting Americans in ways Lehman could not. AIG was one of the largest life and health insurance companies in the country, one of the largest property and casualty insurers, providing insurance to 180,000 small businesses and other corporate entities which together employed about 100 million people. AIG had sold products to protect local and city governments, pension funds, and thousands of public and private companies through guaranteed investment contracts and protection for 401-Ks. And, as problematic, AIG had engaged in a broad range of financial activities that strayed well beyond traditional insurance businesses.

Using a credit rating based on the strength and profitability of its insurance companies, it had become one of the largest providers of complicated financial products in the world. It made hundreds of billions of dollars of financial commitments without the resources to back up those commitments. AIG should have never been allowed to take those risks, but it was. Its insurance regulators in 20 different States, their regulators in other countries responsible for overseeing their international activities, and its holding company supervisor, the Office of Thrift Supervision, did not act to constrain the risks AIG was taking.

Important to recall that the Federal Reserve was given no responsibility and no authority to contain risks that AIG was taking. No one acted to constrain risks taken by AIG, and none of those regulators, in the moment of crisis, had any ability to respond to its failure.

The Government of the United States did not have the ability to seize AIG and wind it down in an orderly way, as the FDIC can and does for banks. Neither the bankruptcy code nor insolvency procedures for insurance companies could have handled the job. And there was no way to draw a line around AIG and prevent its failure from wreaking havoc across the system.

The Federal Reserve was at the center of response to the crisis because it was the only fire station operating. The Federal Reserve faced a terrible choice: to support AIG, putting billions of dollars of taxpayer resources at risk, or to let AIG fail and accept potentially catastrophic damage to the economy. We were not willing to accept such a catastrophe.

So just 4 days after the Federal Reserve was drawn into that crisis, the AIG crisis, we extended AIG a line of credit secured by its insurance businesses. In return, the taxpayer took about an 80 percent stake in the company and began the process of restructuring management and the board and the firm itself. That initial action helped stem the bleeding for a time, but given the massive losses AIG faced, and given the force of the storm moving across the global financial system, it was not enough, and we had to work very quickly almost from the beginning to design and implement a broader, more permanent restructuring.

AIG needed capital, not just a line of credit, and AIG's vulnerability to future losses, to the bleeding of cash had to be reduced.

On November 10th, the Federal Reserve and the Department of Treasury jointly announced a series of steps designed to stabilize the company. The Treasury invested $40 billion of preferred capital under the authority Congress provided the executive branch under the TARP, and the Federal Reserve helped establish and fund two entities, called Maiden Lane II and III, to purchase a range of assets from the company that were threatening AIG's financial solvency. Maiden Lane III, in particular, has been the subject, appropriately, of a range of questions about how we treated firms that had bought these insurance contracts from AIG, and in this effort—and I want to make this very clear—in this effort, our objective was, as always, to get what was the best deal for the American taxpayer. And we faced a number of options.

If we had let AIG default on the contracts, AIG would have gone into bankruptcy, triggering all the disastrous economic consequences we had feared since September that led the Government to act initially. If we had continued to lend AIG money to meet these obligations, its growing debt would have led to a credit rating downgrade, bringing down the firm itself and putting more taxpayer dollars at risk. If we had tried to force counterparties to accept less than they were legally entitled to, market participants would have lost confidence in AIG, leading to the company's collapse. The counterparties could have refused, they could have kept the billions in collateral they had already taken; they could have kept the billions in securities they already had; and they could have sued AIG for breach of contract.

We did not have the luxury of time. We could not engage in protracted negotiations. AIG's financial position was deteriorating rapidly day by day. The prospect of failure was imminent. So we restructured those contracts to stop the bleeding and potentially recover some value for the taxpayer in the future.

Now, although the Government still faces the risk of substantial losses in its overall exposure to AIG, we expect that this particular transaction, the very one that is the heart of so much controversy, will be paid off in full with interest, generating some profit for the American taxpayer.

Now, on November 24th, after President Obama announced his intention to nominate me for Secretary of the Treasury. And after broad consultation with the chairman of the Federal Reserve and others, I decided to stay on as president of the New York Fed on an interim basis, but I withdrew from monetary policy decisions, policies involving individual financial institutions, and day-to-day management of the New York Fed. I had no role before or after November 24th in making decisions regarding what to disclose about the specific financial terms of Maiden Lane II and III and payments to AIG counterparties.

Mr. Chairman, the broad strategy that the Government adopted to contain this financial crisis has been remarkably effective at stemming the crisis, breaking the momentum of the crisis, and repairing the damage, and this has been achieved at much lower cost in taxpayer resources than many people anticipated. Confidence in the basic stability of the American financial system is much stronger today. Borrowing costs for American businesses and consumers, for households, for municipal and State governments have fallen dramatically. The economy is now growing. The support we provided to AIG in the context of the broad strategy to put out this financial fire was essential to achieving this early beginning of healing and recovery.

Banks have already repaid two-thirds of the TARP investments that my predecessor appropriately made. The only support this administration has provided to banks since I took office—to banks—was $7 billion to regional small community banks. More than 75 percent of the emergency Government guarantees that I inherited when I took office have now been shut down and closed at a profit to taxpayers. Over the last year, the expected cost of stabilizing the financial system has fallen by over $400 billion. That is real resources that we can use to meet the many other challenges we face as a country. And if Congress joins with us in adopting the President's proposal for a financial responsibility fee, the American taxpayer will recoup every penny of potential losses under the TARP.

Now, this economy is still in crisis, but because of the Government's actions the American financial system is now in a position where it can provide the credit necessary for economic growth, and that is essential to lay the foundation for job growth and long-term economic prosperity.

Now, let me close by saying this. If you are outraged by AIG—and you should be—if you are outraged by what happened with AIG, then you should be deeply committed to financial reform. The United States of America should never have let institutions like AIG take on a level of risk that could threaten the stability of the financial system. And the Government of the United States should never have been in the position of going into a crisis of this severity without the basic tools able to contain the damage and protect the taxpayer.

So I hope you will join us in working to put in place a strong package of financial reforms that will protect consumers, protect investors, protect the taxpayer, and protect our economy from excessive risk taking by financial institutions.

Mr. Chairman, one final thought. The public servants involved in making these decisions acted solely in the public interest, acted solely in the interest of the American taxpayer. They are dedicated Americans who bring to government service enormous experience and the highest integrity. I would never, and they would never, be part of any decision, any public decision intended for private benefit and not the public interest.

The decisions we made together regarding AIG were enormously consequential; they were terribly difficult; they were the subject of extraordinary controversy within each of the institutions responsible. And for that reason they were subject to enormous care and deliberation. But I believe a fair reading of history, a careful fair reading of history of all the judgments we made, will demonstrate that the actions we took—and I was there—were essential to preventing broader catastrophe, and the solutions we took reduced the ultimate cost of the American taxpayer and the American economy is much stronger today as a result.

Thank you very much.

[The prepared statement of Secretary Geithner follows:]

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Secretary Timothy F. Geithner
Written Testimony
House Committee on Oversight and Government Reform
January 27, 2010

Chairman Towns, Ranking Member Issa, members of the Committee on Oversight and Government Reform, thank you for the opportunity to testify today.

Let me begin by saying how important it is that the government's decisions regarding American International Group, Inc. (AIG), as well as our broader strategy to address this financial crisis, are subject to careful, independent review and analysis.

The decisions regarding AIG have already been the focus of thoughtful examinations by the Government Accountability Office (GAO) and the Treasury Special Inspector General for the Troubled Asset Relief Program (SIGTARP). They have also been the focus of many hearings by this and other committees in Congress. And recently, with my full support, Chairman Bernanke asked the GAO to conduct another review.

I welcome the Committee's attention to this issue. And the Administration will continue to work closely with all relevant oversight bodies to make sure they have the information they need to properly assess the government's actions.

The decision to rescue AIG was exceptionally difficult and enormously consequential.

At that time, our economy stood at the brink. The financial institutions that Americans rely on to protect their savings, help finance their children's education, and help pay their bills were at risk in ways few had ever experienced. The institutions and markets that businesses rely on to make payroll, build inventories, fund new investments, and create new jobs were threatened like at no time since the Great Depression. Across the country, people were rapidly losing confidence in our financial system and in the government's ability to safeguard their economic future.

Action was required. The world was watching. And the government did not have the luxury of time.

The steps the government took to rescue AIG were motivated solely by what we believed to be in the best interests of the American people. We did not act because AIG asked for assistance. We did not act to protect the financial interests of individual institutions. We did not act to help foreign banks. We acted because the consequences of AIG failing at that time, in those circumstances, would have been catastrophic for our economy and for American families and businesses.

The government responded to this crisis in a coordinated way. The Federal Reserve Bank of New York (FRBNY) did not act alone. It did not have the authority to do so. Every action it took was under the direction of the Board of Governors of the Federal Reserve and in cooperation with the Department of the Treasury and the Executive Branch.

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Almost a year and a half removed from that terrible week in September 2008, I believe that the government's strategy regarding AIG was essential to our success in confronting the worst financial crisis in generations. Government support for AIG and our financial system more broadly will ultimately cost taxpayers far less than many feared. And importantly, if Congress adopts the President's proposed Financial Responsibility Fee, American taxpayers will not have to pay one cent for the rescue of our financial system.

The government has not yet repaired all the extensive damage caused by this crisis. For every American out of work, for every family facing foreclosure, and for every small business facing a credit crunch, this recession remains acute. But everyone should realize that because of the actions of the Treasury and the Federal Reserve, the American financial system is now in a position where it can provide the credit necessary for economic growth, not stand in its way. That is an important achievement necessary to lay the foundation for job growth and long-term economic stability.

AIG and the Great Recession

The extraordinary events surrounding AIG took place during what was already the most severe financial crisis the United States and the global economy had seen since the Great Depression. This context is critical to understanding the decisions we made.

Over the two decades preceding the crisis, the financial system had grown rapidly in an environment of economic growth and stability. Ample credit and accommodative monetary policy around the world fueled an unsustainable housing boom in the first half of the last decade, and when the housing market inevitably turned down, starting in early 2006, the pace of mortgage defaults accelerated at an unprecedented rate. By mid-2007, rising mortgage defaults were undermining the performance of many investments held by major financial institutions.

The current financial crisis began in the summer of 2007, gradually increasing in intensity and momentum over the course of the following year. A series of major institutions, including Countrywide Financial, Bear Stearns, and IndyMac collapsed; and Fannie Mae and Freddie Mac, the largest players in the mortgage market, came under severe stress.

By September 2008, for the first time in 80 years, the United States risked a complete collapse of our financial system. Americans were starting to question the safety of their money in the nation's banks, and a growing sense of panic was producing the classic signs of a generalized run. Peoples' trust and confidence in the stability of major institutions, such as AIG, and the capacity of the government to contain the damage was vanishing.

AIG is one of the largest and most complex financial firms in the world. At its peak, AIG had more than $1 trillion in assets, with its core businesses divided into two parts. AIG was the largest provider of conventional insurance in the world, with approximately 75 million individual and corporate customers in over 130 countries. Those insurance activities were organized in separate subsidiaries that were regulated and supervised independently.

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More ominously, AIG's parent holding company, which was largely unregulated, engaged in a broad range of financial activities that strayed well beyond the business of life insurance and property and casualty insurance. Operating in Wilton, Connecticut, and in London and Paris, AIG's Financial Products subsidiary (AIGFP) expanded rapidly into some of the newest, riskiest, and most complex parts of the financial system.

AIG used its strong credit rating, which was based on the strength and profitability of its insurance subsidiaries, to become one of the largest providers of credit and rate-of-return protection for other financial products. Imprudent risk-taking in better times meant that, when the financial cycle turned, AIG had hundreds of billions of dollars in commitments without the capital and liquid assets to back them up.

Such excessive risk-taking should not have been allowed. But it was. Despite regulators in 20 different states being responsible for the primary regulation and supervision of AIG's U.S. insurance subsidiaries, despite AIG's foreign insurance activities being regulated by more than 130 foreign governments, and despite AIG's holding company being subject to supervision by the Office of Thrift Supervision (OTS), no one was adequately aware of what was really going on at AIG.

It is important to remember that the Federal Reserve, under the law, had no role in supervising or regulating AIG, investment banks, or a range of other institutions that were at the leading edge of crisis. But Congress gave the Federal Reserve authority to provide liquidity to the financial system in times of severe stress. Given that responsibility, the Federal Reserve had to act. The Federal Reserve was the only fire station in town.

Three Days in September

On Friday, September 12, 2008, AIG officials informed the Federal Reserve and the Treasury that the company was facing potentially fatal liquidity problems.

As we obtained more details about AIG's financial condition, it became clear they had massive liquidity needs and faced huge losses. Moreover, neither AIG's management nor any of AIG's principal supervisors -- including the state insurance commissioners and the OTS -- understood the magnitude of risks AIG had taken or the threat that AIG posed to the entire financial system.

That weekend, we brought together a team of people from the Federal Reserve, the New York State Insurance Department, and other experts to consider how to respond to AIG's problems. We addressed two basic questions:

1. How would the failure of AIG affect the financial system and the broader economy?
2. What were the options for containing the damage from an AIG failure?

By Sunday night, it became clear that we did not have a willing buyer for Lehman Brothers and that it would have to file for bankruptcy. At that moment, we knew the crisis was about to intensify and spread more broadly. We also knew AIG was highly vulnerable. Nonetheless, even with those new complications, it still seemed inconceivable that the Federal Reserve could or should play any role in preventing AIG's collapse.

The pressures that had caused the failure of Lehman Brothers and had brought AIG to the edge of collapse were symptoms of a broader adjustment moving swiftly through the financial system. In mid-September 2008, virtually all financial institutions were aggressively shedding risk that had been acquired over the long run-up to the crisis. Confidence was fragile and financial firms were trying to shore up their balance sheets by selling risky assets, reducing exposure to other financial institutions, and hoarding cash.

The impending Lehman bankruptcy added to that destructive cycle. Starting Sunday night, we saw not just an escalating run on banks, but also a broad withdrawal of funds from money market funds. These funds, always thought of as one of the safest investments for Americans, had begun trading at a discount. The run on these funds, in turn, severely disrupted the commercial paper market, which was a vital source of funding for many brick and mortar businesses.

The panic spread. Major institutions such as Washington Mutual and Wachovia experienced debilitating deposit withdrawals, eventually collapsed, and were acquired by competitors. These pressures spilled over to virtually all credit markets. Markets for instruments backed by consumer loans, such as auto loans, credit card receivables, and home-equity lines of credit collapsed, and in response banks tightened standards and sharply curtailed the issuance of new loans.

These events had real and immediate economic consequences. State and local governments halted public works projects because they couldn't obtain financing. School construction and renovation projects stopped. Hospitals postponed plans to add beds and equipment. Universities across the nation faced difficulty paying employees. High school students changed plans for college education, which suddenly appeared much more expensive. Ships that transport goods sat empty, in part because trade credit was simply unavailable. Factories were closing and millions of Americans were losing their jobs.

That was the world we were facing as the team of officials from the Federal Reserve and the New York State Insurance Department, working through the weekend, sought to answer those two basic questions about AIG.

How would the failure of AIG affect the financial system and the broader economy?

The team concluded that AIG's failure would be catastrophic. AIG was much larger than Lehman, it was spread across more countries than Lehman, and while it posed many of the same basic risks as Lehman, they were actually greater because of AIG's role as an insurance company.

AIG was one of the largest life and health insurers in the United States. AIG was also one of the largest property and casualty insurers in the United States, providing insurance to 180,000 small businesses and other corporate entities, which employ about 100 million people. History

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suggests that the withdrawal of a major underwriter from a particular market can have large, long-lasting effects on the households and businesses that rely on basic insurance protection.

AIG's failure directly threatened the savings of millions of Americans in ways that the Lehman bankruptcy did not. AIG had provided financial protection to municipalities, pension funds, and other public and private entities through guaranteed investment contracts and products that protect participants in 401(k) retirement plans.

More broadly, if AIG had failed, the crisis almost certainly would have spread to the entire insurance industry. Life insurance posed a particular threat. Many life insurance products are effectively a form of long-term savings. In the wake of a failure of AIG, policy holders could have sought to liquidate life insurance policies underwritten by AIG. Doubts about the value of AIG life insurance products could have generated doubts about similar products provided by other life insurance companies, opening up an entirely new channel of contagion.

And, at that time, with the world economy under severe stress, the failure of a large, global, highly-rated financial institution that had written hundreds of billion dollars of insurance on a range of financial instruments would have dramatically amplified the crisis. Investors around the world would have pulled back from funding, out of fear that other financial institutions would fail as well. Investors would have completely lost confidence in their ability to evaluate the financial sector and distinguish between firms that were viable and those that were not. Financial firms would have been forced into even more dramatic selling of assets.

This damage would have rapidly spread beyond Wall Street. Borrowing costs for businesses would have increased dramatically, the value of pension funds would have fallen even more sharply, and job losses would have skyrocketed. We were witnessing these effects in the wake of Lehman's failure. The effects of the failure of AIG would have been much worse.

What were the options for containing the damage from an AIG failure?

As they were trying to evaluate the potential systemic risk of AIG, the team also explored, at my direction, a range of questions pertaining to containing the damage of AIG's failure: Was there a private sector solution that could have avoided putting taxpayer dollars at risk? Were there effective existing mechanisms for limiting the damage from the failure of an insurance company like AIG? If AIG were to fail, did we have the ability to limit contagion by providing support to other vulnerable institutions?

Because of the scale of AIG's losses and its financial needs, and because of the force of the storm enveloping the rest of the financial system, there was no capacity for a consortium of private firms to find the resources necessary to solve this without government assistance.

The team concluded that there was no effective existing mechanism to limit the damage of an AIG failure. There was no legal tool available to handle the failure of AIG, comparable to the one available to the Federal Deposit Insurance Corporation for managing the orderly wind-down of a troubled bank. In particular, we did not have the ability to quickly separate the stable underlying insurance businesses from the complex and dangerous financial activities carried out primarily by the parent holding company. Experts suggested that achieving that separation would take several years.

Without assistance, the AIG parent holding company would have been forced to file for bankruptcy protection like Lehman Brothers, resulting in default on over $100 billion of debt, as well as trillions of dollars of derivatives. Such a filing would have caused insurance regulators in the United States and around the world to take over AIG's insurance subsidiaries, potentially disrupting households' and businesses' access to basic insurance. And since many of the insurance products that AIG sold were a form of long-term savings, the seizure by local regulators of AIG's insurance subsidiaries could have delayed Americans' access to their savings, potentially triggering a run on other institutions.

Finally, the team concluded that the tools then available to the government to limit contagion in the wake of a failure of AIG to other insurance companies were not likely to be effective.

The Choice

On Monday, September 15, 2008, Fitch Ratings, Moody's Investors Service, and Standard and Poor's downgraded AIG's credit rating, which generated new demands for AIG to post $20 billion in additional collateral at a time when raising new cash was virtually impossible for the company.

It was clear to everyone that AIG did not have the resources to meet such obligations.

That left us with probably the most difficult choice we faced in this entire financial crisis: whether to rescue AIG by putting billions of taxpayer dollars at risk, or to let AIG fail and accept potentially catastrophic damage to the economy.

It is worth repeating that this choice fell to the Federal Reserve because Congress had given it unique responsibility and policy tools to protect the stability of the financial system. No one else could act in the same manner as the Federal Reserve. The only authority the President of the United States had, before Congress authorized the Emergency Economic Stabilization Act (EESA), was to close markets or declare a bank holiday. None of the agencies with supervisory authority over AIG -- the OTS, insurance commissioners, or regulators in Connecticut, London or Paris -- had any tools to help directly meet the funding requirements of AIG. And no one in the federal government had a mechanism, as we do for banks, to provide for the orderly unwinding, dismantling, selling, or liquidating of a global, non-bank financial institution like AIG.

Aware that we were the only ones capable of acting, and convinced that the failure of AIG would be catastrophic for a financial system already in free fall, the Federal Reserve and the Treasury determined that it was in the best interests of the United States to rescue AIG in order to slow the panic and prevent further damage to our economy.

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In that moment, making that wrenching decision, we could not be certain it would work. We could not be confident, given the significant risks, that our actions would be enough or that our initial investment would be our last.

But we knew that not acting would have caused enormous damage, putting the country and the savings of millions of Americans and businesses in greater economic jeopardy. Congress granted the Federal Reserve emergency authority precisely so that the government had some capacity to act to contain a systemic financial crisis. Not to have used that authority at that time would have been deeply irresponsible.

The Restructuring of AIG

On the afternoon of September 16, 2008, the Federal Reserve extended AIG an $85 billion line of credit, secured by a substantial proportion of the assets of AIG. In addition to that collateral, U.S. taxpayers received a 79.9% ownership stake in what was still the world's largest insurance company.

The government's offer required AIG's CEO to step down. Immediately after AIG agreed, the government began the process of changing the Board of Directors. In designing our intervention, the government made sure that there were appropriately tough conditions that put the burden of failure on AIG's existing equity holders and management and started the process of designing a comprehensive restructuring plan.

From the beginning, it was clear that AIG needed a durable restructuring of its balance sheet and operations. The credit provided on September 16th stemmed the bleeding by satisfying AIG's immediate liquidity needs, but that was not enough. The problems at AIG were so deep that we had to design and implement a more permanent restructuring.

Of course, as Federal Reserve and Treasury officials were considering options for AIG in the second half of September and October, we were facing escalating challenges on many fronts. The actions we took to meet these challenges were without precedent. They were exceptionally complicated to design and execute.

Between September 16th and November 10th, the following actions were taken:

- To provide liquidity in U.S. dollars to overseas markets, the Federal Reserve expanded the scope and scale of its swap lines with central banks (Sep. 18, 24, 26; Oct. 14, 29).
- To stop the run on money market funds—key providers of short-term credit in our economy and investment vehicles for millions of Americans—Treasury established the Money Market Guarantee Program (Sep. 19).
- To protect the critical commercial paper market, the Federal Reserve established Asset-Backed Commercial Paper Money Market Fund Liquidity Facility (Sep. 19) and the Commercial Paper Funding Facility (Oct. 7).
- Washington Mutual was closed by the Office of Thrift Supervision and taken over by the FDIC (Sep. 25).

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- Congress passed EESA (Oct. 3). EESA provided Treasury with the authority to purchase or guarantee assets in financial institutions. EESA also increased the limit on FDIC deposit insurance to $250,000 per account.
- As part of an unprecedented coordinated action, the Federal Reserve and other central banks lowered short-term rates (Oct. 8).
- Treasury announced a plan to inject up to $250 billion of capital into U.S. financial institutions using EESA authority (Oct. 14). As the first step of this plan, nine of the largest U.S. banks received $125 billion.
- To stabilize and restore confidence in U.S. financial institutions, the FDIC established the Temporary Liquidity Guarantee Program to guarantee senior bank debt and transaction accounts above $250,000 (Oct. 14).
- To provide additional liquidity for short-term credit markets, the Federal Reserve established the Money Market Investor Funding Facility (Oct. 21).
- The Federal Reserve lowered the Federal Funds rate further, to 1.0 percent (Oct. 29).

In this chaotic environment, AIG remained extremely vulnerable to the ongoing and intensifying financial crisis. Falling asset prices generated both substantial losses on its balance sheet and increases in required payments to AIG's counterparties under the terms of its credit protection contracts. These factors undermined market confidence in AIG and put its investment-grade credit rating again at risk.

Avoiding any downgrade of AIG's credit rating was absolutely essential to sustaining the firm's viability and protecting the taxpayers' investment. Under credit protection contracts that AIG had written and the terms of various funding arrangements, further downgrades would have forced additional payments to AIG's counterparties.

In addition, further rating downgrades of the AIG parent holding company would have significantly undermined confidence in its insurance subsidiaries. People do not buy insurance products from firms they do not believe have the financial capacity to make good on those commitments over the long term – firms that they do not believe will pay out a life insurance policy or compensate a business if a factory burns down. Credit ratings are central to how people judge that viability.

As Federal Reserve and Treasury staff considered options for AIG, it became clear that two things were needed. First, AIG needed capital, not just a line of credit. Second, the vulnerability of AIG's balance sheet to further deterioration in financial conditions generally, and in AIG's own financial position, had to be reduced.

On November 10, 2008, the Federal Reserve and the Department of the Treasury jointly announced a package of actions designed to achieve these goals.

To address AIG's need for capital and to reduce its leverage, the Treasury Department agreed to invest $40 billion in senior preferred stock of AIG under the authority recently granted by EESA. This investment provided new equity capital to AIG, a tool not available to the U.S. government at the time the initial credit line was provided in September 2008.

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To reduce potential demands on AIG's balance sheet, the FRBNY helped establish and fund two new companies. The purpose of these companies was to purchase troubled assets that AIG had either acquired or insured, and to manage those assets for the benefit of the taxpayer. Purchasing those assets removed significant exposure from AIG's balance sheet and helped prevent the company from being downgraded and failing. One company, Maiden Lane II, purchased assets from AIG's insurance subsidiaries. The other company, Maiden Lane III, purchased securities from third parties and insured by AIG's Financial Products subsidiary. This vehicle is described in more detail later.

The Board of Governors of the Federal Reserve and the FRBNY worked closely together in establishing these vehicles. We believed then, and I continue to believe today, that without these transactions, AIG would have failed.

AIG Counterparties

This brings me to the question that has been the source of so much understandable concern and frustration among the American people: the question of how we treated AIG's counterparties when we purchased securities in establishing Maiden Lane III.

While the financial contracts involved were complex, basically, AIG had agreed to insure the value of certain risky securities called multi-sector CDOs. The value of these securities was tied to pools of other assets, mostly subprime mortgages. As the financial crisis intensified, the value of the securities fell sharply and AIG incurred losses on these contracts and had to post collateral or make payments on the insurance.

To help understand this kind of contract, imagine AIG had provided insurance on the value of a tangible asset, such as a house, to the homeowner. If the price of the house fell, AIG would be required to post collateral, or essentially make a payment to the owner, equal to the decline in the value of the house. So, if the house was originally worth $200,000, and fell to $125,000, AIG had to give $75,000 to the homeowner as collateral and would incur a loss of the same amount. In addition, if AIG's credit rating fell, it would have to post even more collateral because the homeowner would be concerned about whether AIG could ultimately pay on the insurance.

The problem was AIG had written billions of dollars of such insurance without sufficient capital. AIG was fine as long as the prices of the assets they were insuring -- housing prices, in the example -- didn't fall, and their own credit rating didn't fall. But if either happened, it would be in trouble. In the fall of 2008, both events occurred. The value of the assets and AIG's credit rating fell, bringing AIG to the brink of bankruptcy.

By August, AIG had already paid out over $16 billion on contracts similar to the ones that Maiden Lane III was designed to address. When the Federal Reserve established the credit facility on September 16th, it knew that there would be substantial further demands of this sort. In the midst of the ongoing financial crisis, the underlying securities were likely to continue to fall in value.

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We faced the following options: let AIG default on these contracts; continue to lend AIG money so it could meet its obligations; or restructure these contracts so that we could stop the hemorrhaging, and potentially recover value for the taxpayers in the future.

If we had let AIG default, it would have gone into bankruptcy, triggering all the disastrous economic consequences we had feared since September.

If we had simply continued to lend AIG money, it could have made these payments, but this would have increased AIG's debt at a time when the rating agencies felt AIG already had too much leverage. Again, any downgrade by the rating agencies would have threatened AIG's viability, driving more uncertainty and panic through the entire financial system. And simply lending AIG the money to make payments could have been an open-ended commitment by taxpayers and would not have given them any assets in return.

Instead, we sought to restructure the contracts. In order to cancel the insurance, we purchased the assets. We paid the fair market value at that time for the assets. Going back to the housing example, we paid $125,000 for a house that AIG had insured at $200,000. The counterparties kept what they already had -- in our example, the $75,000 cash collateral. Taken together, these two amounts essentially equaled par value.

This simple example does not capture the complexity of the transactions. But, essentially what the Federal Reserve did was to purchase these securities (CDOs) with a par value of $62 billion for the purchase price of $27 billion. In designing and implementing this transaction our objective was, as it always is, to get the best deal for the taxpayer. We made judgments about these transactions carefully with the advice of outside counsel and financial experts.

However, we faced constraints. The counterparties held insurance entitling them to full or par value of the contract. We could not credibly threaten not to pay. That meant putting AIG into bankruptcy. At the time, we were working desperately to rebuild confidence in the financial system. Any suggestion that we might let AIG fail would have worked against that vital aim. We could not risk a protracted negotiation. AIG's financial position was deteriorating rapidly and the prospect of a downgrade was imminent.

Some have suggested that the FRBNY should have used its regulatory authority, or some other means, to effectively coerce AIG's counterparties to accept concessions. This was not a viable option either. Once a company refuses to meet its full obligations to a customer, other customers will quickly find other places to do business. If we had sought to force counterparties to accept less than they were legally entitled to, market participants would have lost confidence in AIG and the ratings agencies would have downgraded AIG again. This could have led to the company's collapse, threatened our efforts to rebuild confidence in the financial system, and meant a deeper recession, more financial turmoil, and a much higher cost for American taxpayers.

Operating with these constraints, the FRBNY and AIG initiated discussions with the major counterparties about whether they would be prepared to accept concessions on the prices of the securities. We knew that the likelihood of success was modest. Relatively quickly, and not unexpectedly, we discovered that most firms would not, on any condition, provide such a concession. One said that it was willing, but only if everybody else would agree to equal concessions on their prices.

In the end, the prices paid for the securities were their fair market value. Because of the way the contracts worked, those prices were essentially equal to the difference between the par value of the CDOs and the payments that counterparties had already received.

Since Maiden Lane III purchased these securities, they have generated significant cash flows that have been used to pay down the FRBNY's loan by more than 25 percent. We expect Maiden Lane III to pay the FRBNY back in full and to generate a substantial profit for U.S. taxpayers.

I strongly believe that strategy that the Federal Reserve and the Treasury pursued in establishing Maiden Lane III will generate a better outcome than any alternative.

Disclosure

I had no role in making decisions regarding what to disclose about the specific financial terms of Maiden Lane II and Maiden Lane III, and payments to AIGs counterparties.

On November 24th, President-elect Barack Obama announced that he intended to nominate me to be Secretary of the Treasury. And after consulting with the Chairman of the Federal Reserve Board, the General Counsel of the Federal Reserve Board, the General Counsel of the FRBNY, the Chairman of the Board of Directors of the FRBNY, and the President-elect's advisers, I was asked to stay on as President of the Federal Reserve Bank of New York on an interim basis. We made this judgment, in part, to protect the independence of the Federal Reserve, and, in part, because I was going to be spending the bulk of my time helping shape the President-elect's economic strategy.

Starting on November 24, I withdrew from involvement in monetary policy decision, policies involving individual institutions, and day-to-day management of FRBNY. In accordance with established practice, my colleagues at the Federal Reserve Bank of New York, led by the First Vice President, Christine Cumming, carried out the day-to-day management decisions in close cooperation with their colleagues in at the Federal Reserve Board.

The Broad Strategy

More than a year has passed since the Federal Reserve and Treasury decided to rescue AIG, and substantial challenges remain for our financial system. The economic crisis is not over. Too many Americans face unemployment and too many families face the risk of foreclosure. Many small banks are still experiencing significant losses. That is contributing to a contraction in bank lending, which hurts small businesses especially. Many parts of the financial system remain impaired.

But the broad strategy that the government adopted to contain the financial crisis has been remarkably effective at stemming the crisis and repairing the damage. This has been achieved at

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a much lower cost in terms of taxpayer resources than many people anticipated. I want to highlight some important facts that I don't think are well understood in the Congress or among the American people.

We have already recovered two-thirds of TARP investments in banks that my predecessor appropriately made in the fall of 2008. And we have earned $17 billion on those investments through dividends and warrants. That means that the American government has a dramatically smaller stake in banks than it had when I came into office, and the taxpayer is earning a profit on those investments. The rapid repayment and income from TARP investments in banks are the direct result of government financial policies. In February, the Administration announced a strategy to get private capital to replace public investments and carry the burden of repairing our financial system. The stress tests of our largest financial institutions provided the transparency and confidence necessary for those institutions to raise substantial capital in private markets. Since the results of the stress tests were announced in May, these institutions have raised over $140 billion in high-quality capital and over $60 billion in non-guaranteed unsecured debt.

The Government is terminating the exceptional guarantee programs that were put in place during the darkest days of the fall of 2008. In September, Treasury closed its Money Market Fund Guarantee Program at a profit. At its peak, the program guaranteed $3.2 trillion in assets. October was the last month to issue new debt under the FDIC's Temporary Liquidity Guarantee Program (TLGP). That program has generated roughly $10 billion in net income. The FDIC's TLGP transaction account guarantee program is scheduled to terminate in June. In sum, guarantees through these exceptional programs have been reduced by more than 75 percent since this Administration took office. The Capital Purchase Program, under which the bulk of support to banks was provided, has been closed.

The expected cost of financial stabilization efforts has fallen sharply since last year. In President Obama's February Budget, the projected impact of financial stabilization efforts on the deficit was over $550 billion, including TARP and a reserve in case of continued instability. Today, the Treasury expects that impact will be less than $120 billion. If Congress adopts the President's proposed Financial Responsibility Fee, American taxpayers will not have to pay one penny of loss for the financial rescue.

Over the past year and a half, credit conditions for American consumers and businesses have improved. Rates on consumer and business loans have fallen substantially. Securities markets have reopened. The housing market is more stable.

AIG Today

The situation of AIG today is substantially better than it was six or twelve months ago. AIG's insurance subsidiaries are open for business and generating positive returns. A number of those subsidiaries are attracting attention from external investors. We anticipate that AIG will generate substantial proceeds from the sale of some of those entities. Under the terms of the support we have provided, the first call on the proceeds from any sales of AIG's subsidiaries will be to repay the support that the U.S. government has provided to AIG.

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It is also important to note that AIG has made substantial progress in winding down its Financial Products subsidiary, the division where AIG's problems were concentrated. The gross value of AIGFP derivatives positions are down by more than half since September of 2008, and the company actually generated a profit in the last two quarters for which public information is available.

The U.S. government is still exposed to substantial risk of losses on its investments in AIG. That risk was inevitable, was unavoidable and we cannot know at this point what the scale of those looses will be. While the Federal Reserve's investments in Maiden Lane II and Maiden Lane III are likely to earn a profit, based on what we know now, the government is unlikely to fully recover the direct costs of Treasury's capital investments in AIG. But, today, on the basis of a range of measures, those losses are likely to be substantially lower than we expected even just a few months ago. And I want to emphasize if Congress adopts the President's proposed Financial Responsibility Fee, American taxpayers will not have to pay one cent for the rescue of our financial system.

Our latest audited financial statements show that, as of September 30, 2009, Treasury had invested $43 billion in AIG under TARP. At that time, the "market value" of that investment was $13 billion, implying an expected loss of about $30 billion. We believe that, depending on market conditions and the future performance of AIG's businesses, the actual recovery on the Treasury's Preferred stock could be significantly higher. We are confident that the FRBNY Credit Facility, its loans to Maiden Lane II and Maiden Lane III, and its preferred interests in certain of AIG's subsidiaries will be fully repaid, and FRBNY should earn a profit on its financial support of AIG.

Financial Reform

There are two central lessons from this crisis, both applicable to AIG, that have guided the President's proposals and the legislation now working through Congress to reform our financial system.

First, we need the ability to limit risk-taking for institutions that threaten the overall stability of the system and can cause extraordinary damage to the American economy. We need this ability not just for banks, but for institutions that operate like banks. These non-bank financial institutions have existed alongside banks and yet were not subject to those constraints in this crisis. We also need to make sure that regulators have clear accountability and enforce sensibly-designed constraints on risk.

As I underscored earlier in my testimony, AIG, one of the largest and most complex financial institutions in the world, was allowed to take on an enormous level of risk that eventually threatened our entire financial system. None of the regulators overseeing AIG or any of its subsidiaries understood anything close to the complete scope or scale of that risk. And they clearly failed to contain it. That failure of oversight must not happen again.

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Second, the federal government must have the ability to resolve failing major financial institutions in an orderly manner, with losses absorbed not by taxpayers but by equity holders, unsecured creditors and, if necessary, other large financial institutions.

Under our proposed special resolution authority, a failing firm, such as AIG, would be placed into an FDIC-managed receivership. The purpose of the receivership would be to unwind, dismantle, sell, or liquidate the firm in an orderly way that protects the financial system at the lowest cost to taxpayers.

Shareholders and other providers of regulatory capital of the failing firm would be forced to absorb losses, and managers responsible for the failure would be replaced. Such an approach allows the government to reduce the risk that failure would result in panic by creditors and shareholders of other firms and helps maximize recovery of the value of the firm's assets.

I join the American people and Members of Congress in feeling a deep sense of outrage over this crisis, and over the fact that better tools were not available for the government to confront it. For that reason, we should be working as hard as possible to make sure we put in place a set of financial reforms that would create a safer, more stable financial system, where opportunity can rise, risk can be mitigated, and where there are stronger protections for consumers, investors, and taxpayers.

Conclusion

It is very hard to judge a decision through the prism of hindsight and on the basis of the events that followed. The crisis that unfolded was so severe, damaging the lives of so many Americans, that it's hard for people to imagine how things could have been dramatically worse if AIG had been allowed to default. But I am personally very confident that if we not acted, the crisis would have caused more devastation and would have cost far more money.

Many Americans look at what happened with AIG, and the rest of the financial rescue, and simply ask: Why was it necessary? Why was it fair for the government to take taxpayer money and put it into an institution that had mismanaged itself to the edge of collapse?

The answer is that it was not fair, and it was not something our government should ever have to do. But those Americans, those families and business owners who played by the rules and played no role in giving rise to this recession, should understand that if the government had failed to act, that failure would have unleashed substantially greater damage upon them.

There is an adage the President cites, that if your neighbor's house is burning, even if they've acted irresponsibly, your first priority is to put out the fire before it spreads to your own house.

If we had not put out the fire that was AIG, it would have spread. And if you have any doubt, look at what happened after the failures of Lehman Brothers, Washington Mutual, Wachovia and Countrywide. Look at the impact not just on the savings of Americans, which fell by over 10 trillion dollars, but on the thousands of businesses that had to close, and the millions of workers who were laid off.

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Some people have criticized the actions of the Federal Reserve and Treasury. They argue that we should have done nothing and that government intervention would sow the seeds for an even greater crisis.

I suspect such critics would have agreed with one of my predecessors, who eight decades ago, facing another moment of severe crisis said, "Liquidate labor, liquidate stocks, liquidate the farmer, liquidate real estate. It will purge the rottenness out of the system."

That crisis, of course, was the Great Depression. And the Great Depression became the Great Depression because Andrew Mellon was not alone in his beliefs. In 1930, many people thought that the financial system was going through a necessary adjustment, that the healthy process was to let the fire burn itself out, and that the best thing the government could do was to do nothing.

Today, few believe that. Today, we know that when confronting a severe economic crisis the government must respond with overwhelming force. That is the basic lesson of the Great Depression. That is the basic insight that informed every judgment we made. And that is the reason we are now emerging from a recession and not still in the midst of a second Great Depression.

In confronting this crisis, we learned from the past. Now we must learn from more recent failures, especially those that required AIG's rescue.

If we had stronger supervision and regulation in place, the government could have acted sooner to avert the crisis. If we had better crisis management tools in place, the government would have had better options. If we could have done it any differently, we would have done it differently.

Instead, we had no other choice. That is the basic lesson of this great recession.

In the future, when another generation of Americans confronts a new crisis born of new risks, the question will be whether we provided them the tools we did not have, whether we turned our collective outrage into concrete action, whether we passed comprehensive financial reform.

I hope we will.

Thank you.

Chairman TOWNS. Thank you very much, Mr. Secretary.

Let me begin by asking a couple of questions. Were you involved in any discussions with AIG, or your staff involved, where you discussed what AIG should or should not disclose to the public?

Secretary GEITHNER. Mr. Chairman, as I said, I had no role in making those decisions. But as the record shows, and the record before the committee shows, a large number of people at the Federal Reserve Bank of New York and the Federal Reserve Board in Washington played a very active role in thinking through those difficult choices.

Chairman TOWNS. But I am not sure I got an answer there.

Secretary GEITHNER. Let me say again. I personally played no role before the 24th or after in making those decisions. But you asked whether any employees of the New York Fed did. Of course they did.

Chairman TOWNS. When you were the president of the Federal Reserve Bank of New York, when did you recuse yourself from matters involving specific companies and why did you recuse yourself?

Secretary GEITHNER. On November 24th, the President announced his intention to nominate me as Secretary of the Treasury. That forced me to make a set of decisions about what was appropriate for me to do, given the unique circumstance at that time.

And after consulting with the chairman of the Federal Reserve, with the chairman of my board, with my general counsel, and with a range of other officials, collectively we decided that it was in the best interest of the Fed and the incoming administration for me to remove myself from day-to-day involvement in the Fed's policy issues, to leave that responsibility to my colleagues at the New York Fed, led by the executive, the first vice president of the New York Fed, but not to step down as president.

And we made that decision because we wanted to make sure we were protecting the independence of the Fed and because I was going to be spending, by necessity, a huge part of my time in helping shape the President's economic agenda, and I was not going to be able to give the care and effort needed to carry on running the Fed on a day-to-day basis. Our judgment was that was the best decision at the time. I am confident of that in retrospect. It was unique. It was unique, but I don't think there was a better alternative available.

Chairman TOWNS. Secretary Geithner, I don't think AIG's counterparties should have been paid 100 cents on the dollar, because in this email we have here—it is on the screen as well—you had some interest in how much the counterparties were owed. Please tell the committee what impact the counterparties' exposure had on your decision to pay 100 cents on the dollar.

Secretary GEITHNER. Mr. Chairman, that played no role in our decision. As I said in my opening statement and as I have testified before, we had to make a difficult choice about what was going to prevent the failure of the firm at least cost to the taxpayer. If we had broken those contracts, if AIG had not paid them in full, if we had threatened default, if we had imposed haircuts, if we had selectively imposed haircuts, that would have brought about a downgrade in its rating, the firm would not have been able to operate, and it would have collapsed. It was because of those choices we took the path we did, to restructure the contracts and leave the taxpayer with some of the potential upside in those securities.

Now, judging what is systemic and why a failure of AIG might matter for the system as a whole is a very difficult judgment to make; there is no black and white choice in that context. But our judgment was, as I said in my testimony, that AIG's collapse would have dramatically magnified all the effects you saw in the immediate aftermath of Lehman's failure, and in some ways they would have been more consequential because they would have spread to a set of insurance businesses, and that would have been much worse for the country. So we were guided by a simple but terrible choice: how best to prevent default at least cost to the taxpayer.

Chairman TOWNS. Thank you very much, Mr. Secretary.

I now yield to the gentleman from California, the ranking member, Congressman Issa, for 5 minutes.

Mr. ISSA. Thank you, Mr. Chairman. I am going to pick up pretty much where you left off.

Secretary Geithner, I think you have answered that you played no role in the decision to not disclose the full payment, the 100 percent payment, to the counterparties, that you were not part of what some of us have called a cover-up. Is that right?

Secretary GEITHNER. Absolutely.

Mr. ISSA. OK. Let me followup, then. If, after November 24th, you were not involved in any activity, then one more just to be clear. Did you ever become involved with the Federal Reserve's disclosure decision with respect to AIG counterparty claims after your nomination as Treasury Secretary? In other words, have you ever participated or questioned or stayed involved with that?

Secretary GEITHNER. No, I did not.

Mr. ISSA. Well, from what we were given by the Fed, could we put up slide 1? This email from you says—to William Dudley, your replacement, on March 2009—OK, it is easier to read on the screen—Where are you on the AIG counterparty disclosure issue? Long after you left you made this email. What was it about and what was the answer?

Secretary GEITHNER. Well, Congressman, as you know, this question of disclosure was the subject of a huge amount of controversy and most people——

Mr. ISSA. You think?

Secretary GEITHNER. Yes. That is what my son says, and I agree with you. And I think most people feel as you do, they said why shouldn't it be disclosed? Why shouldn't it be disclosed? And, as you know, in March—which I think, if I am not mistaken, was the time of this email——

Mr. ISSA. Yes, March 15th.

Secretary GEITHNER [continuing]. It had been subject of testimony by the vice chairman of the Federal Reserve, and the Federal Reserve was facing a huge amount of pressure and attention over what it disclosed. So I assume I was doing what you might expect in that context in asking them where were they, were they going to change their position.

Mr. ISSA. OK. Well, then, following up on your continued involvement looking at them, where are you on this? Do you believe that there should be full disclosure, as the President has said that these kinds of instruments should be public, that essentially, they be like any other instrument, the details of which should be available broadly?

Secretary GEITHNER. Congressman, I believe deeply that trust and confidence in the financial system requires disclosure and transparency. I believe that trust and confidence in the Government requires that our actions be subject to full exposure and review by careful independent analysis. And I have been very, very supportive, since I came into office and before, to making sure we were bringing an unprecedented level of disclosure to the transparency around the actions of the Government. I will just give you a few examples.

When I came into office, we put the financial terms of all of the transactions we undertook under the TARP in the public domain for everyone to see. One of the reasons our financial strategy has been successful in bringing a measure of stability back to our system is we compelled the largest institutions in the country to subject their balance sheets to a level of disclosure——

Mr. ISSA. Well, Secretary, I appreciate what you have been doing as Treasury Secretary, but I have in front of me from the Fed, marked confidential, the details of who benefited, who got these benefits, and currently it is locked up until 2018 by an order that wasn't negotiated and final until May of this year—May of last year, long after you were obviously able to be involved, that locks up the public knowing, and these are assets the American people have paid for in full, right? Do you believe that we should know about these?

Secretary GEITHNER. Congressman, that is an issue that I think you need to direct to the New York Fed and to the SEC.

Mr. ISSA. OK. Well——

Secretary GEITHNER. You asked me a question that I didn't quite get a chance to answer before, which is you said what was my view, in effect——

Mr. ISSA. Yes.

Secretary GEITHNER [continuing]. Of what the Fed ultimately did. It is very important to recognize that the Fed did, in March 2009, fully release information of the counterparties and the details of that transaction, and based on what I know, I thought the decision was appropriate then. Now, I know a lot of people have said shouldn't that have come sooner I think reasonable people could come to that judgment, but I did not stand in their shoes.

Mr. ISSA. Now, as a member and the head of the New York Fed, and also, I guess, broadly a member of the board generally, until you were sworn in——

Mr. KUCINICH [presiding]. The gentleman's time has expired.

Mr. ISSA. I will just finish up this one question, Mr. Chairman, very quickly.

You were aware that Chairman Bernanke, in fact, had in front of him from the staff a report that said AIG should be allowed to go bankrupt, which was then held back on September 16th based on his decision on September 15th not to disclose this for a broad vote of the board, weren't you?

Secretary GEITHNER. I am not aware of the email that you are referring to, but I am aware of the——

Mr. KUCINICH. The witness may answer the question and then we are going to move on to the next questioner.

Secretary GEITHNER. Thank you.

Every decision we made in the days before September 16th and afterwards were enormously controversial——

Mr. ISSA. No, no.

Mr. KUCINICH. The gentleman's time has expired.

Mr. ISSA. I understand.

Mr. KUCINICH. The Chair recognizes Mr. Kanjorski.

Mr. ISSA. I would ask unanimous consent to just get an answer to the question. It would be very quick.

Mr. KUCINICH. Well, each Member has 5 minutes. We will—without objection, the witness can answer the question, then we will move.

Mr. ISSA. The only question we want is were you aware of that? And if you weren't, do you think you should have been aware of that for a vote on September 16th? That's all.

Secretary GEITHNER. Well, I was aware that there was enormous concern both in the New York Fed and at the Federal Reserve Board about the choices we were confronting. As I said, there is nothing more controversial and difficult than I think any we faced in this context, and I think it should be reassuring and no surprise that those actions—and the record will show that those actions were the subject of enormous debate, and they were the subject of debate before the 16th and afterwards, and every time we faced the possibility of having to do more, we all stepped back and said do we really need to do that, does that make sense? And that is a good thing for the country, that you had people willing to debate that and argue it forcefully.

Mr. KUCINICH. Thank you.

The Chair recognizes Mr. Kanjorski.

Mr. KANJORSKI. Thank you very much, Mr. Chairman.

Mr. Secretary, there is a famous expression. I think it comes from one of the fine poets of our era: We have come to bury Caesar, not to praise him. And I hope you appreciate the role of Caesar that you are playing today. But it made me think about the fact that last Sunday I watched the ball game and in the closing moments of the ball game the quarterback made a tremendous decision to pass the football and got intercepted. And, as a result, the opposing team took the ball down the field, kicked a field goal, and won the game. And I convened several meetings in New York after that game and met extensively on Monday and Tuesday, and we have concluded that he just did the absolute worst thing that he could have done. Every one of us at those meetings would have made the correct decision after the fact.

I think the point I am trying to make is I do share some of the sympathies with you because I was on the committee and the task force that was working with the Secretary and with the chairman of the Federal Reserve when the crisis occurred, and I caution some of the members I think even of this committee were AWOL for the votes that we needed to authorize the saving of the American economy.

As I have heard your testimony, you have come to the conclusion that if the rescue package had not been passed by the Congress of the United States authorizing the Secretary and the President to take extraordinary action and commit hundreds of billions of dollars of taxpayers' money, we wouldn't be sitting in this room today. We probably wouldn't be operating under the Constitution that was saved as a result of that precipitous action taken in a very short period of time. Is that relatively correct?

Secretary GEITHNER. I completely agree. And those Members of Congress on both sides of the aisle that voted to authorize that action did the right and the necessary and the courageous thing, and they made it possible for my predecessor and the Federal Reserve to start to stabilize this thing. And it would not have been possible without that authority and without that legislation.

Mr. KANJORSKI. I appreciate that. I sometimes—as a matter of fact, I took that argument to the White House at that time. If you remember, the President was not as outspoken, and I always was convinced that in a democracy such as ours, transparency, both in bad news and dangerous news, must be shared with the people. And part of the problem at that time, we didn't share that news. And even to today, most people in this audience and most people throughout America have no idea how close we came to total annihilation and disaster. Is that correct?

Secretary GEITHNER. That is my view. I think for the first time since the Great Depression you were seeing a full scale run on the financial system. People were taking their savings out of banks. They wondered whether a dollar was a dollar; whether their dollar in a money market fund would be worth a dollar. They worried about whether a dollar lent to a AAA company would be worth a dollar. It was a basic calamitous breakdown in the fabric of our system and no recovery would have been possible without starting to stabilize the system and stem the bleeding, and that was something that could not happen without the authority that, as I said, many people in this room, many people on both sides of the aisle voted to approve.

Mr. KANJORSKI. Am I correct that there were discussions held at the highest echelons of the U.S. Government and the Congress at that very time as to whether or not law and order could be secured in the United States if we did not take precipitous actions to assure the people that the economic markets in the United States and the world would be held secure?

Secretary GEITHNER. I was not in the executive branch at that time, so I can't speak to that, but it would not surprise me if that was the case. Again, this was the gravest crisis we had seen since the Great Depression. It was not going to solve itself. Many people advocated we should let it burn itself out, but that would have been catastrophic for the economy. We are still living with the consequence of the damage and the wreckage. The scale of the challenges we face today as an economy are rooted in that crisis and they illustrate the force of the pressure and the momentum that was already—we were already living with in August of that summer.

Mr. KANJORSKI. All the decisions made in those fateful 2 weeks weren't the correct decisions, were they?

Secretary GEITHNER. Oh, Congressman, I think every day about things we could have done differently and done early, and I think a great strength of this country is that people in the Congress, in independent oversight bodies, in the financial crisis commission were all going to take a cold, hard look at everything that was done, and that will give us a better basis——

Mr. KUCINICH. The gentleman's time has expired. You may continue with your answer.

Secretary GEITHNER [continuing]. And that will give us a better basis for fixing this mess and preventing it from happening again, and we will cooperate fully in all that effort.

Mr. KANJORSKI. Thank you, Mr. Chairman.

Mr. KUCINICH. I thank the gentleman.

The Chair recognizes Mr. Burton.

Mr. BURTON. Thank you, Mr. Chairman.

Your counsel, one of your counsels, James Bergen, said on March the 12th, I don't know if there is any way to manage it so that Congress won't ask for it or, if they do, won't release it. Does he work for you, or did he work for you?

Secretary GEITHNER. Yes, he did.

Mr. BURTON. Does your legal counsel have the authority to make comments and decisions without your knowledge?

Secretary GEITHNER. Of course. But——

Mr. BURTON. Regarding something of this import?

Secretary GEITHNER. Well, as president and CEO of the New York Fed, of course, I was ultimately responsible——

Mr. BURTON. This doesn't require a long dissertation.

Secretary GEITHNER. No, it's not a long——

Mr. BURTON. All I want to know is do they have the authority to make these kinds of comments and decisions without you knowing about it.

Secretary GEITHNER. Of course.

Mr. BURTON. On November the 11th, when you were still at the Fed, an internal memo said, as a matter of course, we do not want to disclose that the concession is at par unless absolutely necessary. Are you familiar with that memo?

Secretary GEITHNER. Not with that email. As I said, I was not involved in decisions about what to disclose about the individual transactions or the names of counterparties. But I have enormous trust and confidence in the integrity and judgment of people who were.

Mr. BURTON. On March the 15th, after that, we had up on the board there a few minutes ago the email to Mr. Dudley that said where are you on the counterparty disclosure issue? And Dudley responded, my understanding is that it is in train and could come out as early as today. Are you familiar with that?

Secretary GEITHNER. I don't recall his response, and I didn't recall my email until you put it in front of him, but now I see it.

Mr. BURTON. You don't remember that?

Secretary GEITHNER. No, I don't, but I do remember at the time there was still enormous building pressure on the Fed to disclose and they did disclose.

Mr. BURTON. But you still maintain that you weren't involved in any of this?

Secretary GEITHNER. Yes, absolutely.

Mr. BURTON. Were you aware that all of these organizations around the world, Societe Generale, Goldman Sachs, Merrill Lynch, Deutsche Bank, UBS, were all getting 100 cents on the dollar?

Secretary GEITHNER. Absolutely.

Mr. BURTON. You were aware of all that? Why wasn't this disclosed back in November, when you were head of the Fed?

Secretary GEITHNER. Well, again, that is a question you need to direct to the people who were responsible for that judgment.

Mr. BURTON. Well, you were the head of the Fed.

Secretary GEITHNER. I was the head of the Federal Reserve Bank in New York until I was confirmed by the Senate for this job.

Mr. BURTON. Why wouldn't this have been disclosed by you back then? I mean, you are saying that—what, was this a group that made the decision?

Secretary GEITHNER. Congressman, I don't know how to say it any differently, but when the President announced his intention to nominate me, I withdrew, appropriately, from a whole range of policies decisions of the Federal Reserve Bank of New York in part to protect the Fed, in part so I could do my job of helping the President prepare for how to fix the mess we inherited. Now, because of that I was not involved in those decisions. But I want to say the people who made those decisions did so——

Mr. BURTON. This happened on November the 11th, before you withdrew.

Secretary GEITHNER. What happened on November——

Mr. BURTON. This knowledge.

Secretary GEITHNER. Oh. Mr. Chairman, as I said in my testimony, I wasn't——

Mr. BURTON. Why wasn't it disclosed back then?

Secretary GEITHNER. Well, we didn't face that choice then. I was directly involved in the judgments that we collectively made——

Mr. BURTON. You didn't face the choice back then?

Secretary GEITHNER. No, we didn't. No. But the choice that I was deeply involved in, fully support, believe was the right choice was the decision to restructure these contracts in a way that was better for the taxpayer and prevented the fall of the company. I was fully supportive of that, fully aware of that.

Mr. BURTON. It stretches credulity for us to believe that you had no role in this and didn't know anything about it when your attorneys and people that worked for you were sending emails all around the place, and you were the head of the Fed and you didn't know anything about it? It just doesn't make any sense to me, and I think a lot of my colleagues feel the same way.

Secretary GEITHNER. Congressman, I was president of the New York Fed throughout that time. I was—we were involved, as you know, in an extraordinary complicated range of things.

Mr. BURTON. But this is major stuff.

Secretary GEITHNER. The decisions around AIG were major and hugely consequential, and they were done with enormous care and judgment. But the choices around disclosure, which understandably are the focus of so much attention, are not judgments I could speak to.

Mr. BURTON. Let me just finish by asking you this. Do you think that there ought to be an annual audit of the Fed?

Secretary GEITHNER. I am very supportive——

Mr. KUCINICH. The gentleman's time expired, but, Mr. Secretary, you may answer the question.

Secretary GEITHNER. I am very supportive, as part of financial reform, of trying to make sure that the Fed is subject to an aduate level of transparency and disclosure and oversight, and the chairman of the Federal Reserve has worked with many Members in Congress in helping shape reforms that would achieve that outcome.

Mr. BURTON. I'll take that as a yes.

Secretary GEITHNER. In doing that, though——

Mr. BURTON. I'll take that as a yes.

Secretary GEITHNER. In doing that, though, I want to be—it is very important we protect the independence of the Federal monetary policy issues. It would be a deep mistake for the country, a grave mistake for the country to threaten that independence.

Mr. KUCINICH. The Chair recognizes Mr. Cummings. You may proceed.

Mr. CUMMINGS. Secretary Geithner, I don't know whether you realize this, but it was the Democrats that asked for this hearing. I specifically asked for this hearing. Did you know that?

Secretary GEITHNER. I believe I did know that.

Mr. CUMMINGS. And let me tell you that when I asked for the hearing, I must tell you that I was extremely concerned and I was questioning whether you had acted appropriately. And I think anyone who read headlines back then, when this hearing was requested, would have come to at least the question mark.

Now, you sat here a few moments ago and you swore that you would tell the truth, is that correct?

Secretary GEITHNER. I did.

Mr. CUMMINGS. Is that correct?

Secretary GEITHNER. I did.

Mr. CUMMINGS. And I assume that the statement, your written statement is a statement which you would also swear to?

Secretary GEITHNER. Absolutely.

Mr. CUMMINGS. And I can tell you that as I read your written statement, I am trying to figure out, as far as the initial getting involved with AIG and what you all did, I don't know what anybody else would have done. I don't think we had a choice, or that you had a choice. So let me say that I think we did the right thing there.

Now, this is where it gets sticky. We also have a situation, Secretary Geithner, where the American people are concerned that a lot is being done for Wall Street, but not enough being done for Main Street. You understand that?

Secretary GEITHNER. Absolutely.

Mr. CUMMINGS. And one of the interesting things is that you talked about how, if you had not taken the action from the beginning, how it might have affected Main Street, the constituents of all 435 Members. Can you tell us, if you hadn't taken the action, how might it would affect students in my district or businesses or whatever? Can you tell us that? Because I don't think that is getting through.

Secretary GEITHNER. Thousands of more factories would have closed their doors. Millions more Americans would have lost their jobs. The value of America's houses and savings would have fallen even further than they did at that time. People would have rushed to take their money out of banks. It would have brought about utter collapse. I don't know a better way to say it than that.

And if people wonder whether that was true, I think all they have to do is look back at what actually happened in the fall of 2008, and you saw the value of American savings fall by almost 40 percent; trillions of dollars in lost wealth. Millions of Americans lost their homes; thousands and thousands of businesses had to close.

That is what happens when you let a financial crisis get out of control. Governments should never let that happen, but if they don't act—and this is a very important thing for people to understand. People think it is unfair for the Government to act to rescue a financial system. But you cannot help an economy recover, you can't create jobs, you can't preserve the value of people's savings without a functioning financial system.

Mr. CUMMINGS. Another moment, when we requested the hearing, that I was concerned about was this counterparties. As you probably know, I, along with 26 other Members of Congress, requested that SIGTARP, Barofsky, look into that whole issue, and there have been comments that the capital levels of the counterparties were tenuous, and had they not been paid in full, they risked collapse. Was this a real possibility?

Secretary GEITHNER. In my judgment, that was not the most important risk posed by AIG. AIG's failure would have posed some direct losses on those major banks, but those losses themselves were not the issue; they would not have been significant. The threat to the system—and this was a threat to all institutions operating—was the threat of collapse of the system as a whole. And if AIG had failed, you would have seen a crisis spread to insurance companies around the world and you would have seen investors, depositors, creditors, pull back from every financial institution in the world, and that would have brought a much more precipitous collapse in all financial values.

Mr. CUMMINGS. My time is running out. Just real quick. When the public has so much invested in a company, isn't it better to err on the side of transparency, Mr. Secretary, as opposed to keeping things secret?

Secretary GEITHNER. Of course. Of course.

Mr. CUMMINGS. So what would push the decision to not be as transparent? I mean, what would cause that?

Secretary GEITHNER. There are very few cases where it is necessary for there to be either a lag in disclosure or some gap. I am not sure how to—the best way to explain this, but like in national security, like in law enforcement——

Mr. KUCINICH. The gentleman's time has expired, but you can conclude your answer.

Secretary GEITHNER [continuing]. Like in the protection of confidential supervisory information, but also to protect the taxpayer, there are some areas in which you need to be careful about how you manage that. That is a discussion, though, you should have with my colleagues at the Fed; they are in a better position to answer it. But we would not want to disclose information that would be bad for the taxpayer, make it harder for the taxpayer to recoup our investments.

But, in general, Congressman, I completely agree that transparency and disclosure are essential, the American people deserve it and we have been very effective in bringing an unprecedented level of security to all the basic actions we took in this financial crisis, an unprecedented level of transparency in disclosure.

Mr. KUCINICH. Thank you.

Mr. CUMMINGS. Thank you very much, Mr. Chairman.

Mr. KUCINICH. Thank you.

The Chair recognizes Mr. Mica.

Mr. MICA. Thank you, Mr. Chairman.

Mr. Secretary, it is kind of interesting the way you have framed your testimony and your involvement in some of these decisions before the committee today. I think you have tried to give the impression that you had to do what you had to do because of the financial situation. That is pretty much what you have said, right?

Secretary GEITHNER. Oh, absolutely.

Mr. MICA. Thank you. And then you used the term—you kept using the term we made decisions together. Then you said a dividing line of November 24th. Is that when you received word that you were going to be nominated for Treasury Secretary?

Secretary GEITHNER. That is when the announcement was made.

Mr. MICA. Yes. So you have tried to distance yourself from decisions that were made before that, but, in fact——

Secretary GEITHNER. No, no, I have not tried to distance—I take pride and full responsibility for all those decisions.

Mr. MICA. OK. Then you also were aware when the New York Federal Reserve Board ultimately selected, on November 3, 2008, to purchase the underlying assets?

Secretary GEITHNER. Oh, absolutely.

Mr. MICA. You were.

Secretary GEITHNER. And, again, as I said, I take pride in that decision.

Mr. MICA. Also, you had no knowledge of any cover-up, right, or intent not to give full information and disclosure.

Secretary GEITHNER. Of course not.

Mr. MICA. Of course not. So you took credit for the decision but not the cover-up.

Secretary GEITHNER. No, no——

Mr. MICA. Then you distance yourself from any cover-up before November 24th. And then, of course, you were out of the picture from November 24th forward, is that correct?

Secretary GEITHNER. Congressman, I am not trying to distance myself from anything. I will take complete responsibility for decisions I played a role in shaping or was part of shaping, including all decisions up to the 24th on this case. And I am happy to take responsibility for all decisions I have made since then too.

Mr. MICA. Then you were aware of 100 cents on a dollar bailout.

Secretary GEITHNER. Absolutely.

Mr. MICA. Absolutely. And the risk that was posed by that offer. So you knew about that, but you weren't attempting to cover up, that is your testimony today?

Secretary GEITHNER. Of course not.

Mr. MICA. OK. So I believe either you made a bad decision there or in fact there was the attempt to cover up one of the biggest bailouts, back-door bailouts, in history. Now, you have tried to frame it as you did it because you did it in the interest of the people and the failure of the system. I am telling you I believe these are lame excuses. Either you were in charge and did the wrong thing or you participated in the wrong thing. To me, it appears like when you were being confirmed, a lot of controversy surrounded your not paying your taxes. You gave lame excuses then. I believe you're giving lame excuses now.

My final question is why shouldn't we ask for your resignation as Secretary of the Treasury? I didn't think you should have been Secretary of the Treasury when it was disclosed that you didn't pay your taxes, because that is the highest financial responsibility position in the U.S. Government. So why shouldn't you step down now?

Secretary GEITHNER. That is your right. That is your right to that opinion. I have worked in public service all my life. I have never been a politician. I have served my country as carefully and ably as I can, and it is a great privilege for me to work with this President to help repair the damage that was here when we took office. And I will do so as long as he asks me to do so to the best of my ability, with great pride in this country and in him.

Mr. MICA. Again, I think you're punting the blame and I think you're trying to position yourself as——

Secretary GEITHNER. Congressman, you don't know me very well.

Mr. MICA [continuing]. And yet——

Secretary GEITHNER. You don't know me very well. I will take——

Mr. MICA [continuing]. I believe that we are not getting the whole story; we are getting a lame story in a monumental back-door decision of bailout for which the American taxpayers will stay on the hook for huge amounts of money. Even by estimates of the Treasury Department, there will be billions of dollars from this deal, which either you should have been overseeing, and you said you had knowledge of and you failed to take some steps to further protect the taxpayer interest. You were either incompetent on the job or you were not doing your job and knew what was taking place and tried to conceal it, and I think that is grounds for your removal.

Secretary GEITHNER. Congressman, I was there. I know what I was responsible for. I take full responsibility and, as I said, great pride in those judgments.

Mr. KUCINICH. The gentleman's time has expired, but the Secretary may answer the question as he sees fit.

Mr. MICA. He takes great pride in those judgments.

Secretary GEITHNER. I do. I take great pride in those judgments. And people have a right to disagree with them and they have a right to go back and look at them with great care and analysis. And I hope you will give the same care and judgment to looking at those decisions in retrospect, with the benefit of hindsight, that we gave in making those decisions at that time.

Mr. KUCINICH. I thank the gentleman.

It is my time to ask questions and I am yielding myself 5 minutes.

Mr. Geithner, the New York Fed agreed to Goldman Sachs' demands for billions to settle its counterparty claims with AIG, 100 cents on a dollar, but for more than a year before that Goldman and AIG had been locked into a dispute over that money and Goldman believed it would lose up to $2.5 billion if AIG defaulted. Did you know at the time that Goldman Sachs had concluded it would not receive 100 cents on the dollar from AIG in the event of default?

Secretary GEITHNER. I did not know, and I don't know whether that is true or not.

Mr. KUCINICH. Goldman had said publicly that they didn't need the Government's money, that it was fully hedged and would not have been materially affected if AIG had defaulted. But that turns out to be disingenuous. Committee investigators have learned that Goldman's supplemental insurance policy would not pay in the event that the U.S. Government bailed out AIG. Goldman's protection would pay only in the event AIG defaulted. Goldman had not anticipated the Government bailout and so hadn't put that contingency into the terms of its contracts. That failure put Goldman at real risk of losing the entire amount of disputed money once the Government rescued AIG.

Did you have any knowledge at the time, did Lloyd Blankfein or anyone at Goldman ever admit to you or anyone working under you that Goldman Sachs was not fully hedged in the event the Government took over AIG, and that Goldman was at risk of losing at least $2.5 billion if the Government bailed out AIG and imposed less than 100 cents on the dollar on counterparties?

Secretary GEITHNER. Congressman, I am not aware—and I don't see how I could have been aware—of the precise details of the hedging strategies of all those firms to the event of a default by AIG. But we made a very careful effort to try to assess, working with the supervisors of all the institutions at exposure to AIG about what their economic exposure would be——

Mr. KUCINICH. Had you talked to Lloyd Blankfein, for example, about this? Do you remember talking to him?

Secretary GEITHNER. In the Goldman Sachs case in particular, because there were a lot of press reports that were consequential in this case, I did ask them directly what their exposure was and I asked them to show me what their internal information system reports showed about that exposure.

Mr. KUCINICH. The committee, if I may, is going to have a series of questions to submit to you in writing——

Secretary GEITHNER. Happy to answer those questions.

Mr. KUCINICH [continuing]. So that you will be given an opportunity to have an extensive answer on this point.

Secretary GEITHNER. Happy to answer those questions.

Mr. KUCINICH. Now, Mr. Secretary, once the Government stepped in, there was only one way for Goldman Sachs to get any piece of the $2.5 billion, and that was if the New York Fed voluntarily agreed to give it to them. Now, if the New York Fed had fought for taxpayers, Goldman would have lost money it didn't have any hope of recovering. In spite of public statements to the contrary, the New York Fed had a lot of leverage, a lot of leverage, to negotiate a reduction, which would have saved taxpayers billions. But, instead, the New York Fed took Goldman Sachs' position in its dispute with AIG and settled it fully with taxpayers' money.

Now, Mr. Geithner, under normal circumstances, Goldman Sachs would have had to sue AIG in court to recover the disputed $2.5 billion, and they would have settled for something less than that. Isn't it true that the New York Fed gave Goldman Sachs a better deal than it could have ever expected from AIG or any market player at any other time?

Secretary GEITHNER. Congressman, if we had the ability, like we have for normal companies seized, to put them through bankruptcy, if we had the ability, like we have for banks, to put them into an orderly wind-down process like quasi-bankruptcy, we could have done many things. But under the laws of the land, we did not have the ability, so we faced a very simple choice: let AIG default or prevent it. And there was no way—financial, legal, or otherwise—we could have imposed haircuts, selectively default on any of those institutions, without the risk of downgrade and default, and that is the only reason——

Mr. KUCINICH. I just want to say, Mr. Secretary, since when does saving the system require the taxpayers to give a better deal than the market would normally deliver? Yet, that is what the New York Fed did. The Government gave Goldman Sachs more than Goldman Sachs had any right to expect, while at the same time giving no financial relief whatever to millions of Americans facing a foreclosure crisis. And if that doesn't illustrate what the New York Fed thought who it was working for, I don't know what does.

Secretary GEITHNER. Congressman——

Mr. KUCINICH. You may respond and then my time has expired.

Secretary GEITHNER. Congressman, that is not true, and it is unfair to the public servants——

Mr. KUCINICH. What is not true?

Secretary GEITHNER. What you just said.

Mr. KUCINICH. What? What isn't true?

Secretary GEITHNER. It is not true that the actions we took in AIG were for the benefit of anybody but the millions of Americans who, at that point, were suffering from the worst financial crisis since the Great Depression. The only way to help reduce that damage, protect that damage, was to fix the system and prevent the catastrophic failure that would have made that crisis worse. That is the only motive that underpinned these actions by the Government.

Mr. KUCINICH. I thank the gentleman. My time has expired.

The Chair recognizes Mr. Duncan.

Mr. DUNCAN. Thank you, Mr. Chairman.

Mr. Secretary, you talked about looking at these events with the benefit of hindsight. Two men who did were Peter Boone, who is a researcher at the London School of Economics, and Simon Johnson, a professor at MIT——

Mr. KUCINICH. Could the gentleman be closer to the mic so we can hear you? Thank you.

Mr. DUNCAN [continuing]. Simon Johnson, a professor at MIT Sloan School of Management, and they wrote in the New Republic magazine, in the September 23rd issue, "The Fed may well have mitigated our current crisis by sowing the seeds for the next one," and they say, in fact, the Fed has exacerbated the possibility of another similar or even larger crisis. In fact, the way they put it, they say, "As a result, unless real reform happens soon, we face the prospect of another bubble burst bailout cycle that will be even more dangerous than the one we have just been through."

Now, I assume you know that the American people are very, very angry about these bailouts and the bonuses and salaries that have come about through what most people see as a big government-big business duopoly, and they feel like this big government-big business duopoly has been manipulated in such a way as to allow just mind-boggling salaries and bonuses, and allowed very few elitists at the top to come out like robber barons to an extent really not known in American history. Because of big government, through the Federal Reserve system, our free market system was not allowed to operate, and it seems to most of us that it is not capitalism when Government uses billions and billions of taxpayer money to prop up a very few well-connected firms.

Now, that leads me to two questions. One, has the Treasury informed any of these financial giants that we will not follow too-big-to-fail policies in the future? And, second, do you think we should limit these salaries, these ridiculously excessive salaries and bonuses, that are even being talked about even today in any of these firms that got taxpayer bailout funds?

Secretary GEITHNER. Congressman, that was a very thoughtful question. You asked exactly the right question. In a financial crisis, you face this tragic choice: you can let it try to burn itself out and let the damage spread to all sorts of innocent victims, or you can act to prevent it, knowing that acting to prevent it will create the risk that in the future investors will expect the Government to step in in the future and save firms from the consequences of failure. That is the dilemma at the heart of strategy in financial crisis.

To stand back and let it burn is irresponsible. It is what happened in the Great Depression. It almost happened to this country. The moral, just, pragmatic, fair choice—and this should be true if you are a Republican or a Democrat—is to act to protect the innocent.

But, as you said wisely, by definition, that creates the risk we sow the seeds for future crises, and that is why, in the financial reform problem, we all have a huge stake in trying to make sure we not just limit risk-taking in the future, but that investors and equity holders and creditors and managers and executives do not run these firms with the expectations the Government will be there again. And that is why it is so important we put in place types of bankruptcy mechanisms that we have now for banks but we do not have for institutions like AIG.

Now, absolutely, we have made clear in public, in crystal clear terms, in reform proposals that are now moving through the Congress, that we need to end this expectation of too-big-to-fail and

Government assistance. And if you look at what we have done since we came to office, we have moved very aggressively to pull the Government out of these institutions, to make sure we are not in these institutions a day longer than is necessary, to replace the public capital with private capital; and we have done that by forcing disclosure and forcing firms to recapitalize with private money, precisely because we want to limit the scale of the Government's involvement and end this exceptional period as quickly as we could.

And that strategy has been very, very effective in ways that people on the right and the left should welcome. On the right, it means that the Government is out much more quickly than anybody expected; on the left, people should know, with confidence now, that we have far more resources now available to help address the long-term challenges we face as a country to reduce our long-term deficits and try to meet the things that we have to do to fix what was broken in this country.

But you asked a very good question and I agree very much with the thrust of your concern.

Mr. DUNCAN. Well, that was a good answer to my first question, but my second question was do you think bonuses and salaries should be limited in any way in these firms that did receive Government bailout money?

Secretary GEITHNER. I think——

Mr. KUCINICH. The gentleman's time has expired, but please answer the question.

Secretary GEITHNER. I think what happened to compensation across this country and in the financial system was terribly catastrophic. It is judged—it came in the wave of a huge increase in income inequality in the United States over decades. In the financial system it was much worse and it was much more consequential because it helped encourage a level of risk-taking that again brought the system to the edge of collapse.

So it is deeply important in the public interest of the country that Congress legislate reforms that will change how bankers are paid. Government can't do it alone, though. Shareholders and their representatives on the boards of these firms have to bring about much tougher limits on how firms are paid. I think that is very important to do and I hope we will have support from the Congress in making sure we have the basis for doing that.

Mr. KUCINICH. I thank the gentleman.

The Chair recognizes Mr. Lynch of Massachusetts.

Mr. LYNCH. Thank you, Mr. Chairman.

Mr. Secretary, I am well aware of your family's commitment to public service, so it makes it more difficult, in a sense, to ask these questions, but I honestly feel that the conduct of yourself and Mr. Paulson were not consistently on the side of the American taxpayer, and I will explain why. I will give you two examples.

We had the situation with Bear Stearns. The circumstances are the same: the world is on the brink; we have a disaster; we are worried about the whole system melting down. With your support and Mr. Paulson, Mr. Bernanke, we forced Bear Stearns shareholders from a position, I think it was a high of $172 a share in January. We forced them down to $2 a share because the American taxpayer money was in the bailout. And that was something that was supported by the Fed, by Treasury because we felt that because the taxpayer was bailing them out, that the shareholders of Bear Stearns should not be held harmless.

Now, you have a different situation here, slightly different. A number of weeks later, where we have AIG going under. And these are credit default swaps, so the money going into AIG is going right out to the counterparties. This is a pass-through. And the folks on the other side are Goldman Sachs, largely. That is the principal beneficiary of all this. And we don't negotiate a nickel, not a cent off of what they are getting. You are in the same position. You are supposed to be negotiating on behalf of the American people.

Now, you are saying, oh, the regulations were different. Let me tell you something. We were changing the rules and regulations every single day. We were taking action, the Fed, under 13.3 under extraordinary circumstances. You had every opportunity, every opportunity to weigh in on behalf of the American people and make these people take a new deal, make them take a haircut. You scalped the folks on Bear Stearns; 2 cents on a dollar they got; 2 cents on a dollar. The folks at Goldman Sachs got 100 cents on a dollar. And that is just unacceptable. Totally unacceptable. You had the opportunity and I just think it was a terrible decision on your part, and also on Mr. Paulson's part; and he is up later and we will talk to him.

Secretary GEITHNER. Congressman——

Mr. LYNCH. How do you expect to—look—and the thing about changing over to the Obama administration, you get the same people who are relying on you, the American taxpayer when you are in one job and the American taxpayer is relying on you in the other job. I don't see a conflict. I really don't. You could have done the right thing by those people, by the American taxpayer, because their money was being put into this deal.

Secretary GEITHNER. Congressman——

Mr. LYNCH. And it just stinks to the high heaven what happened here——

Secretary GEITHNER. Congressman——

Mr. LYNCH —and I don't like the obfuscation. And to top it all off, the disclosure was not there. The disclosure was not there at the proper time to tell the American people and tell this Congress what was going on, and that is just inexcusable and it makes me doubt, it makes me doubt your commitment to the American people, it makes me doubt Mr. Paulson's commitment to the American people, and I think the commitment to Goldman Sachs trumped the responsibility that our officials had to the American people.

Secretary GEITHNER. Congressman, I respect your opinion. I know you hold those opinions strongly, but I completely disagree. The American taxpayer would not have been better off if the Government had made it possible for equity holders in Bear Stearns to get more money. The American taxpayer would not have been better off if we had let AIG default. None of us did anything out of any concern for——

Mr. LYNCH. There is a difference between giving them 100 cents on a dollar and letting them default. This was a new game. You were creating new facilities every week to help folks.

Secretary GEITHNER. We were. We were because——

Mr. LYNCH. We were letting people go to the discount window that never had an opportunity to do that. We were changing the rules day by day and we had the banks at a position where we could have exercised a lot of leverage, and you chose not to do it.

Secretary GEITHNER. I disagree.

Mr. LYNCH. You chose not to do it.

Secretary GEITHNER. I disagree with you——

Mr. LYNCH. And that doesn't mean we have to pay them 100 cents on the dollar or we let them fail. There are increments here and we never used that leverage.

Secretary GEITHNER. Not in this case.

Mr. LYNCH. In this case exactly.

Secretary GEITHNER. No, not in this case.

Mr. LYNCH. Under 13.3 we could have taken different steps than we took here.

Secretary GEITHNER. Thirteen three had nothing to do with this in this particular case. What 13.3 was—and this is important for people to understand—13.3 was authority given to the Federal Reserve to protect the financial system from broad-based runs. It gave us the authority only to lend against collateral to make sure that firms that were solvent could fund. We did that because of the catastrophic damage caused by decades of previous financial crises. We used that authority because we thought there was no other choice and we used that authority appropriately.

Mr. LYNCH. Look, let me just say——

Chairman TOWNS [presiding]. The gentleman's——

Mr. LYNCH. Reclaiming my time.

When Hank Paulson pulled nine banks into a room and said you're taking bailout money, that was extraordinary action, OK?

Chairman TOWNS. The gentleman's time has expired. I must move on.

Mr. LYNCH. He could have done the same thing negotiating a better rate on behalf of the American taxpayer.

I yield back.

Secretary GEITHNER. If it would have been possible, we would have done it. Why would I want to be sitting here before you today having to defend actions that look like they could have been avoided? There is nobody who was part of that decision that would not have done that if it would have been possible. I try to be as careful as I can in explaining the reasons why it was not possible, but it comes down to this basic tragic choice: If you are prepared to default, you can impose haircuts; if you can't accept the consequences of default, you do not have any leverage. It would have been vastly more expensive to the American taxpayer. It would have been much more damaging to people you and I care about, people you and I wake up every day worrying about, if we had let that firm fail. There was no choice between default and the restructuring of those contracts, and they left the taxpayer better off——

Mr. LYNCH. There was no shared sacrifice, no shared sacrifice for Goldman Sachs and the American people.

Chairman TOWNS. Would the gentleman from Massachusetts yield? The gentleman's time has expired and I now call on Mr. Turner from Ohio.

Mr. TURNER. Thank you, Mr. Chairman.

Mr. Geithner, in answer to one of my colleagues, you previously stated that you had never been a politician. I want to assure you, from your answers today, that you are absolutely a politician. And let me tell you one of the examples——

Secretary GEITHNER. Do you mean that as a compliment or not? I can't tell.

Mr. TURNER. Let me tell you one of the answers that troubled me about the issue in your written testimony of the team concluded AIG's failure would be catastrophic. You go on to talk about the insurance arms of AIG. Now, this is not the first hearing that this committee has had or other committees, and you know that we are aware of the independence of the insurance arms of AIG. We have Maurice Greenberg, a former chairman and CEO of AIG, said, "to the best of my knowledge, the problems that came to a head this year did not originate in AIG's insurance businesses, which remain fundamentally strong."

We had the head of the New York State Insurance Department, Superintendent Eric Dinallo, came in and said this, "before I go further, I would like to make one critical point. It is important for everyone, and especially policy holders in AIG insurance companies, to understand that the insurance companies, which are regulated by New York and other States, are solvent and have the funds to pay any policy holders' claims; they had independent reserves."

You did not bail out the insurance companies of AIG, correct? They didn't need it. You bailed out the parent, right?

Secretary GEITHNER. Yes. But if the parent had defaulted——

Mr. TURNER. So when we go through your answer of if AIG had failed, the catastrophic effect of all of the insurance companies that were under AIG, they weren't bailed out by you.

Secretary GEITHNER. No, that's not true. But maybe this is helpful to go back a little bit. When AIG came to us that weekend—remember, the Fed is not their regulator; the Fed had no responsibility or authority over how they ran their business, that was the province of other regulators. It was inconceivable to me that this was a problem we were going to have to try to solve, and we got all the people we could, including the New York State insurance commissioner and his staff, other people to look at and explain to us——

Mr. TURNER. Let's pause a second. Did you bail out the life insurance arms of AIG?

Secretary GEITHNER. Those insurance companies——

Mr. TURNER. Did you bail out the life insurance arms of AIG?

Secretary GEITHNER. Well, again, I wouldn't use that term. The actions we took helped prevent——

Mr. TURNER. Did you bail out the health insurance arms of AIG?

Secretary GEITHNER. Again, the actions we took to prevent default of the firm protected those companies from the risk of failure.

Mr. TURNER. Mr. Geithner, the testimony we have received previously, from those who were looking at those arms, was that they were substantially sound, so the catastrophic effects that you list certainly are something that we would all have been concerned about, but nonetheless——

Secretary GEITHNER. I disagree completely. People can look at this and they can come to different judgments, but the people who were responsible for looking at those insurance companies frankly had no idea of the risk—and you could not separate those companies from the companies that had taken terrible risk. The tragic thing in the structure of the company was they were so closely linked they couldn't separate them.

Why would we have not, if it had been possible to separate the place that was taking the firm down, to separate that cleanly, separate them from this? We would have done that in a second. And, in fact, much of what the management of the firm is trying to do today, still, 15 months later, is designed to achieve that objective. But they were tightly connected; they could not have been separated. And the insurance supervisors who were responsible for the individual firms did not know the extent to which the financial basis of the insurance companies was so connected to the holding company and the AIFP that had taken all those risks.

Mr. TURNER. Mr. Secretary, as you were going through the bailouts and as we look to the counterparties and the funds that were received, one of the biggest concerns that I have had through all of this process is that I believe that when it all becomes public—and it hasn't all become public yet because we don't have everything from you—that this may turn out to be the largest theft in history, that there were parties that were participating, through mortgage-backed securities and through other credit default swaps, into defrauding Mr. and Mrs. American Citizen on Main Street who was receiving a loan on their home that was negative in loan-to-value ratio and also had a greater risk than was being reported as the mortgage-backed securities and credit default swaps were passed up the chain.

Do you have any information of AIG knowing that the loan-to-value ratios were inflated and that the risks were being understated? Because I truly believe that throughout this system that brought down the systematic mortgage crisis system process, that there was a significant amount of defrauding going on and that people need to be held accountable, and I don't think in your system, where you are bailing out, you are taking into consideration those that were bad actors.

Secretary GEITHNER. I completely agree that this country allowed, under the laws of the land, a terrible erosion in underwriting standards, a terrible amount of predation and abusive practices in mortgage lending and consumer finance. We should never have let that happen. And I hope you will join with us in trying to pass reforms to prevent that from happening again.

Mr. TURNER. But in your bailout——

Chairman TOWNS. The gentleman's time has expired. Hold it a second.

Let me just say something to all the Members. You know, right now we have like 30-some Members who still have not had an opportunity to question, so we are going to have to stick to the time. So I want you to respect that. I mean, I noticed a couple of situations where you are going over, but I am saying to you that when the red light comes on, that is it.

We are now moving to Mr. Quigley of Ohio. Illinois, I am sorry. Mr. Quigley of Illinois. Is he here?

Ms. Kaptur of Ohio.

Ms. KAPTUR. Thank you, Mr. Chairman.

Mr. Secretary, welcome. Can you provide for the record a copy of the recusal agreement that you signed when you were at the New York Fed?

Secretary GEITHNER. I did not sign a recusal agreement; I withdrew from day-to-day management, operations, and policies of the New York Fed, and my colleagues, both in Washington and in New York, can attest to that.

Ms. KAPTUR. So there was no formal agreement?

Secretary GEITHNER. No. As I said in my testimony, what I did is I withdrew from—and this was very important to do. Again, no precedent for this, a sitting president of the New York Fed being nominated to be Secretary of the Treasury. And I withdrew from, after carefully consulting with my colleagues, from involvement in monetary policy decisions. I did not go to the FOMC meeting in December, and I withdrew from all decisions about the individual cases involving the financial system and from day-to-day management; and that was the right thing to do at that time.

Ms. KAPTUR. Thank you. Thank you for clarifying that.

No. 2, a lot of people think that the president of the New York Fed works for the U.S. Government, but, in fact, you work for the private banks that elected you.

Secretary GEITHNER. No, that is not true.

Ms. KAPTUR. Can you provide for the record the names of the handful of bankers on the board of the New York Fed that elected you in 2003?

Secretary GEITHNER. That is a matter of public record and of course——

Ms. KAPTUR. It was 2003?

Secretary GEITHNER. Of course we can do that.

Ms. KAPTUR. Thank you very much.

Secretary GEITHNER. But, Congresswoman, can I just say what you said was not true. I work in the public interest. Officials of the Federal Reserve work for the public interest and they work for the government.

Ms. KAPTUR. But the people don't elect you. The heads of the Feds around the country don't elect you; it is the individuals who sit on the board of the New York Fed that elect you. Is that correct?

Secretary GEITHNER. It is slightly more complicated than that. What the Congress did in setting up the Fed is set up a system where the presidents of the regional reserve banks are elected by their board, but it requires the approval of the chairman of the board of Governors in Washington for them to serve. So it is a delicate balance of checks and balances and Congress designed that system.

Ms. KAPTUR. But it is largely private banks that elected you, and I would like you to provide that for the record, please.

Secretary GEITHNER. Oh, absolutely. It is a matter of public record.

Ms. KAPTUR. The Cleveland Fed is not equal to the New York Fed, so I am very interested in your answer to the record.

No. 3, Goldman Sachs was the largest domestic recipient of funds in this AIG counterparty arrangement. Let me ask you, now as Treasury Secretary, your chief of staff is the gatekeeper for access to you. Could you please provide his name?

Secretary GEITHNER. His name is Mark Patterson.

Ms. KAPTUR. Thank you. And for whom did he work before you selected him as your chief of staff?

Secretary GEITHNER. He worked for the President's transition team.

Ms. KAPTUR. No, before that. Which Wall Street firm did he work for?

Secretary GEITHNER. And before that—again, this is a matter of public record and you know the answer to this question—he worked for Goldman Sachs.

Ms. KAPTUR. Thank you very much.

Secretary GEITHNER. But——

Ms. KAPTUR. You answered my question, Mr. Secretary.

Secretary GEITHNER. No, Congresswoman——

Ms. KAPTUR. Now, let me say this. The AIG transaction——

Secretary GEITHNER. What you are doing is——

Ms. KAPTUR. You have answered the question. You have answered the question. Thank you. The AIG transaction was disturbing to many observers. Why did our Government not require the bank creditors to take the lead and bear some of the costs in any plan to stabilize AIG? You, in effect, nationalized the company and let the bank creditors off the hook. Why did you, as president of the New York Fed, not work out an arrangement to remove the London unit from the company rather than allowing the unit to infect the entire company?

Secretary GEITHNER. If we had had the types of bankruptcy procedures we have for banks, it is possible that ultimately we could have done that. And if it would have been easy and cheaper for the taxpayer for us to separate the riskiest parts of the firm from the healthy, profitable insurance companies, we would do that; and, in fact, that is the core of the restructuring strategy the company is now undertaking. But that choice was not available to us at the time. If it had been possible, of course we would have done that. But because we did not have the tools that we have under bankruptcy, we did not have that choice.

Ms. KAPTUR. Thank you, Mr. Secretary. Your phone logs from the subpoenaed material this committee requested, which I would like to insert in the record, show between September 14th——

Chairman TOWNS. Without objection, so ordered.

[The information referred to follows:]

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
12/31/2008			[redacted]	
	6:03 PM	Scott Alvarez		talked
	4:20 PM	Mary Goodman		talked
	4:14 PM	Alan Fitzpane		talked
	2:43 PM	Tom Donilon		talked
	2:40 PM	Joel Klein		talked
	2:15 PM	Mike Froman		talked
	1:54 PM	Barney Frank		talked
	1:15 PM	Annette Nazareth		talked
	1:00 PM	Dick Beattie		talked
	12:30 PM	John Dugan		talked
	12:15 PM	Steve Rattner		talked
	12:00 Noon	Stuart Levey		talked
	11:30 AM	Bill Wilkins		talked
	11:29 AM	Jamie Rubin		talked
	11:00 AM	Richard Skillman		talked
	10:45 AM	May Lee		talked
	8:53 AM	Ben Bernanke		talked
	8:17 AM	Ian Solomon		talked
12/30/2008				
	10:01 AM	Hank Paulson		talked
	9:18 AM	Annette Nazareth		talked
12/29/2008	6:16PM	Ralph Schlosstein		talked
	6:03PM	Lee Sachs		talked
	5:52PM	Tom Donilon		talked
	5:36PM	Hank Paulson		talked
	3:32PM	David Cohen		talked
	3:10PM	Lee Sachs		talked
	3:04PM	Ben Bernanke		talked
	2:32PM	Lee Myerson		talked
		Mike Froman		talked
	1:06PM	Josh Steiner		talked
	1:00PM	Lee Sachs		talked
	12:53PM	Alan Krueger		talked
	12:33PM	conference call with Konrad Alt		talked
	12:23 PM	Lee Sachs		talked
	12:11PM	Larry Katz		talked
	12:09PM	Lee Sachs		talked
	11:42AM	Mike Froman		talked
	11:25AM	Ian Solomon		talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
			[redacted]	
12/26/2008				
12/24/2008				
	2:19 PM	Lee Sachs		Talked
	1:49 PM	Ian Solomon		Talked
	12:09 PM	Ian Solomon		Talked
12/23/2008	5:58 PM	Lewis Alexander		Talked
	5:40 PM	Annette Nazareth		Talked
	5:31 PM	Les Samuels		Talked
	3:45 PM	Meg McConnell		Talked
	1:54PM	Sen Corker		Talked
	1:30PM	John Dugan		Talked
	10:28 AM	Josh Steiner		Talked
	10:07 AM	Steve Thieke		Talked
	9:42 AM	Mike Froman		Talked
	9:36 AM	Tom Donilon		Talked
	9:02 AM	Lee Sachs		Talked
	8:58 AM	Pat Parkinson		Talked
	8:44 AM	Ben Bernanke		Talked
12/22/2008	11:52 AM	Jean Claude Trichet		Talked
12/19/2008	??	Secretary Paulson		Talked
	3:15 PM	Senator John Sununu (R - NH)		Talked
12/18/2008	5:48 PM	Nancy Killefer		Talked
	5:42 PM	Jake Siewert		Talked
	12:30 PM	Hank Paulson		Talked
	11:38 AM	Stuart Levey		Talked
	10:23 AM	Ian Solomon		Talked
	10:20 AM	Chairman Bernanke		Talked
12/17/2008	3:24 PM	Annette Nazareth		Talked
	3:15 PM	Chairman Bernanke		Talked - says Paige
	1:00 PM	Secretary Paulson		Talked - says Paige
12/16/2008	12:39 AM	Sara Aviel		Talked
	10:23 AM	Ian Solomon		Talked
	10:27 AM	Annette Nazareth		Talked
	10:24 AM	David Dreyer		Talked
12/15/2008	3:05 PM	Richard Neiman, NYS Bnkg Dpt.		WLR spoke with him on 12/15
	12:36 PM	Les Samuels		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	9:45 AM	Pat Parkinson	[redacted]	Talked
12/12/2008	11:56 AM	Annette Nazareth		Talked
12/11/2008	7:34 PM	Jim Leach		Talked
	7:02 PM	Jamie Rubin		Talked
	6:45 PM	Larry Summers		Talked
	6:20 PM	Hank Paulson		Talked
	5:16 PM	Chairman Bernanke		Talked
	4:28 PM	Tom Nides		Talked
	3:41 PM	Rahm Emanuel		Talked
	2:51 PM	Didem Nisanci		Talked
		Hank Paulson		Talked
		Jim Leach		Talked
	12:47 PM	Mario Draghi		Talked
	12:18 PM	Josh Steiner		Talked
	11:53 AM	Stanley Fischer		Talked
	11:15 AM	Larry Summers		Talked
		Phil Schiliro (Obama related)		
12/10/2008	6:26 PM	Jeffrey Goldstein		Talked
	6:13 PM	Tim Collins		Talked
	6:08 PM	Chairman Sheila Bair		Talked
	5:57 PM	Jamie Dimon		Talked
	5:51 PM	Michele Smith		Talked
12/8/2008	8:58 AM	Stephanie Cutter		Talked
12/5/2008	5:39 PM	Bill Dudley		Talked
	3:37 PM	Denis Hughes		Talked
	2:05 PM	Bill Dudley		Talked
	12:12 PM	Stephanie Cutter		Talked
	12:02 PM	Michael Froman		Talked
	10:47 AM	Jack Lew		Talked
	10:44 AM	Stephanie Cutter		Talked
	9:30 AM	Les Samuels		Talked
	7:04 AM	Kevin Lane		Talked
12/4/2008	5:50 PM	Calvin Mitchell		Talked
	10:19 AM	Mayor Bloomberg		Talked
12/3/2008	6:50 PM	Sylvia Matthews		Talked
	6:27 PM	Ralph Schlosstein		Talked
	4:41 PM	Rahm Emanuel		Talked
12/2/2008	several	Ian Solomon		Talked
	1:25 PM	Dr. Alan Greenspan		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	7:52 AM	Hank Paulson	[redacted]	Talked
12/1/2008	6:59 PM	Larry Fink		Talked
	4:32 PM	Dr. Agustin Carstens, Mexico		Talked
	4:29 PM	Jerry Corrigan		Talked
	12:07 PM	Gov. David Paterson		Talked
	10:29 AM	Michael Silva		Talked
				Talked

61

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
11/26/2008	6:15 PM?	Mark Patterson	[redacted]	Talked
	5:45 PM	Larry Summers	[redacted]	Talked
	5:33 PM	A. B. Culvahause (Tom Donilon's Partner)	[redacted]	Talked
	4:06 PM	Tim Collins	[redacted]	Talked
	3:53 PM	Christine Varney (Mike Froman's Office)	[redacted]	Talked
	3:49 PM	Stu Eizenstat	[redacted]	Talked
	3:47 PM	Andrew Williams	[redacted]	Talked
	3:45 PM	Simon Potter	[redacted]	Talked
	3:42 PM	Senator Charles Schumer	[redacted]	Talked
	3:31 PM	Bob Corker, US Senator	[redacted]	Talked
	3:21 PM	Congressman Rangel	[redacted]	Talked
	3:18 PM	David Wilcox	[redacted]	Talked
	3:03 PM	Charles Wait	[redacted]	Talked
	2:53 PM	Art Angulo	[redacted]	Talked
	2:06 PM	Mark Patterson,	[redacted]	Talked
	1:57 PM	Chairman Bernanke	[redacted]	Talked
	1:45 PM	Les Samuels	[redacted]	Talked
	12:30 PM	Mario Draghi	[redacted]	Talked
	12:21 PM	Chancellor Darling - British Finance Minister	[redacted]	Talked
	12:03 PM	Stephanie Cutter (w/Andrew Williams)	[redacted]	Talked
11/25/2008	6:50PM	Hank Paulson	[redacted]	Talked
	5:16PM	Larry Fink	[redacted]	Talked
	5:07PM	Tom Baxter	[redacted]	Talked
	4:44PM	Larry Summers	[redacted]	Talked
	4:38PM	Charlie Bish	[redacted]	Talked
	4:34PM	Les Samuels	[redacted]	Talked
	4:31PM	Larry Summers	[redacted]	Talked
	4:17PM	Lee Sachs	[redacted]	Talked
	4:06PM	Rahm Emanuel	[redacted]	Talked
	3:50PM	Lee Sachs	[redacted]	Talked
	3:48PM	Bob Kimmit	[redacted]	Talked
	3:41PM	Don Graham	[redacted]	Talked
	3:31PM	Bob Kimmit	[redacted]	Talked
	2:27PM	Larry Summers	[redacted]	Talked
	2:20PM	Calvin Mitchell	[redacted]	Talked
11/24/2008	6:51PM	Josh Steiner	[redacted]	Talked
	6:40PM	Josh Steiner	[redacted]	Talked
	6:23PM	Lee Sachs	[redacted]	Talked
	6:22PM	Congressman Rangel	[redacted]	office will CB 11/25
	6:13PM	Congressman Bainer	[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	6:01PM	Meg McConnell	[redacted]	Talked
	5:40PM	Hank Paulson	[redacted]	Talked
	4:25PM	Terry Checki	[redacted]	Talked
	4:24PM	Ben Bernanke	[redacted]	Talked
	9:19AM	Secretary Paulson	[redacted]	Talked
11/23/2008	8:42 PM	Meg McConnell	[redacted]	Talked
	8:39 PM	Michael Froman, Citigroup	[redacted]	Talked
	8:16 PM	Chairman Bernanke	[redacted]	Talked
	7:58 PM	Steve Friedman	[redacted]	Talked
	7:38 PM	Secretary Paulson	[redacted]	Talked
	7:29 PM	Meg McConnell	[redacted]	Talked
	7:28 PM	Secretary Paulson	[redacted]	Talked
	6:55 PM	Secretary Paulson	[redacted]	Talked
	5:11 PM	Secretary Paulson	[redacted]	Talked
	3:37 PM	Secretary Paulson	[redacted]	Talked
	3:22 PM	Josh Steiner	[redacted]	Talked
	2:35 AM	Larry Summers	[redacted]	Talked
	2:24 AM	Chairman Bernanke	[redacted]	Talked
	2:17 PM	Michele Smith	[redacted]	Talked
	1:49 PM	Bob Rubin	[redacted]	Talked
	1:23 PM	Michael Froman, Citigroup	[redacted]	Talked
	12:48 PM	Rahm Emanuel	[redacted]	Talked
	10:57 AM	Mona Stuphen	[redacted]	Talked
	10:55 AM	Secretary Paulson	[redacted]	Talked
	10:19 AM	Steve Friedman	[redacted]	Talked
	10:06 AM	Michael Held	[redacted]	Talked
			[redacted]	
11/21/2008	7:21 PM	Secretary Paulson	[redacted]	Talked
	7:17 PM	Dan Tarullo	[redacted]	Talked
	4:55 PM	Carl Turnipseed	[redacted]	Talked
	4:53 PM	Prime Minister Gordon Brown (UK)	[redacted]	Talked
	4:10 PM	Mona Sutphen	[redacted]	Talked
	3:59 PM	Dan Jester	[redacted]	Talked
	3:35 PM	Dan Tarullo	[redacted]	Talked
	2:23 PM	Secretary Paulson	[redacted]	Talked
	1:48 PM	Dan Tarullo	[redacted]	Talked
	12:16 PM	Secretary Paulson	[redacted]	Talked
	12:30 PM	c/with Congressman Rahm Emanuel, et al	[redacted]	Talked
	10:55 AM	Chairman Bernanke	[redacted]	Talked
	10:41 AM	Chairman Bernanke	[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
		Dan Taurullo	[redacted]	Talked
	10:38 AM	Charlie Bish		Talked
	10:07 AM	Vikram Pandit		Talked
	10:00 AM	Congressman Rahm Emanuel		Talked
	9:44 AM	Lee Sachs		Talked
	9:34 AM	Don Kohn		Talked
	9:21 AM	Shelia Biar		Talked
	8:45 AM	Kevin Warsh		Talked
	8:19 AM	Secretary Paulson		Talked
	7:54 AM	Chairman Bernanke		Talked
11/20/2008	6:57 PM	Michael Froman, Citigroup		Talked
	6:46 PM	Ken Chenault, American Express		Talked
	6:35 PM	Secretary Paulson		Talked
	6:32 PM	Jeff Immelt		Talked
	6:31 PM	Chairman Bernanke		Talked
	6:24 PM	Secretary Paulson		Talked
	6:23 PM	Jamie Dimon		Talked
	6:19 PM	Secretary Paulson		Talked
	6:11 PM	Chairman Bernanke		Talked
	5:02 PM	Bob Hoyt		Talked
	4:59 PM	Calvin Mitchell		Talked
	2:57 PM	Steve Keenan		Talked
	2:20 PM	Josh Steiner		Talked
	2:04 PM	Art Angulo		Talked
	1:53 PM	Axel Weber		Talked
	1:18 PM	David McCormick		Talked
	1:12 PM	Secretary Paulson		Talked
	1:02 PM	John Mack		Talked
	12:53 PM	Jamie Dimon		Talked
	12:32 PM	Lewis Kaden		Talked
	12:28 PM	Don Graham		Talked
	11:46 AM	Secretary Paulson		Talked
	10:56 AM	Don Kohn		Talked
	10:52 AM	John Dugan		Talked
	10:06 AM	Larry Summers		Talked
	9:56 AM	Sheila Bair		Talked
	9:49 AM	Jerry Speyer		Talked
	9:37 AM	Congressman Rahm Emanuel		Talked
	9:26 AM	Secretary Paulson		Talked
	9:07 AM	Secretary Paulson		Talked
	8:53 AM	Larry Summers		Talked

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TALK SHEET

Talked DATE	TIME	CALLER	[redacted]	MESSAGE
	6:33 AM	Secretary Paulson	[redacted]	Talked
11/19/2008	6:58 PM	Lee Sachs	[redacted]	Talked
	6:44 PM	Congressman Rahm Emanuel	[redacted]	Talked
	6:28 PM	John Dugan	[redacted]	Talked
	6:24 PM	Lloyd Blanklein	[redacted]	Talked
	6:17 PM	Secretary Paulson	[redacted]	Talked
	5:26 PM	Secretary Paulson	[redacted]	Talked
	4:59 PM	Secretary Paulson	[redacted]	Talked
	4:25 PM	Lloyd Blankfein	[redacted]	Talked
	4:23 PM	Diane Ashley	[redacted]	Talked
	3:59 PM	Ned Kelly	[redacted]	Talked
	3:48 PM	Dan Jester	[redacted]	Talked
	3:02 PM	Vikram Pandit	[redacted]	Talked
	2:54 PM	Larry Summers	[redacted]	Talked
	2:50 PM	Secretary Paulson	[redacted]	Talked
	1:51 PM	Ralph Schlosstein	[redacted]	Talked
	12:51 PM	Larry Fink	[redacted]	Talked
	12:33 PM	James Hamilton	[redacted]	Talked
	12:22 PM	Calvin Mitchell	[redacted]	Talked
	11:39 AM	Michael Kelly (Special Agent)	[redacted]	Talked
	10:12 AM	Art Angulo	[redacted]	Talked
	10:01 AM	Chairman Bernanke	[redacted]	Talked
	9:55 AM	Secretary Paulson	[redacted]	Talked
	9:51 AM	Robert Wilmers	[redacted]	Talked
	9:46 AM	Josh Steiner	[redacted]	Talked
	9:40 AM	Josh Steiner	[redacted]	Talked
	9:40 AM	Secretary Paulson	[redacted]	Talked
	9:12 AM	Larry Summers	[redacted]	Talked
	9:00 AM	Congressman Rahm Emanuel	[redacted]	Talked
	8:34 AM	Bob Scully, Morgan Stanley	[redacted]	Talked
11/18/2008	6:33 PM	Jeff Lacker	[redacted]	Talked
	6:18 PM	Secretary Paulson	[redacted]	Talked
	6:09 PM	Ray Young, General Motors	[redacted]	Talked
	6:02 PM	Sandy Weill	[redacted]	Talked
	4:40 PM	Dan Jester	[redacted]	Talked
	4:57 PM	Steve Pearlstein, Wash Post	[redacted]	Talked
	4:52 PM	Lewis Kaden	[redacted]	Talked
	4:26 PM	Bob Rubin	[redacted]	Talked
	3:53 PM	Secretary Paulson	[redacted]	Talked
	12:57 PM	Chairman Bernanke	[redacted]	Talked
	12:36 PM	Philipp Hildebrand	[redacted]	Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	12:29 PM	Roger Altman	[redacted]	Talked
	12:21 PM	Michael Heid		Talked
	12:09 PM	Congressman Rahm Emanuel		Talked
	11:55 AM	Josh Steiner		Talked
11/17/2008	??	Lee Sachs		Talked
	4:43PM	Rick Wagoner - CEO and Chairman of GM		Talked (as per TFG -lp)
	1:16PM	Mario Draghi		Talked
	12:58 PM	Steve Friedman		Talked
	12:54PM	Congressman Rahm Emanuel		Talked
	7:58 AM	Hank Paulson		Talked
11/14/2008	2:15 PM	Roger Altman		Talked
	3:10 PM	Josh Steiner		Talked
	1:47 PM	Kevin Warsh		Talked
	12:30 PM	Larry Summers		Talked
	12:08 PM	Andrew Cuomo		Talked
	11:40 AM	Rodgin Cohen		Talked
	11:27 AM	Michael Nelson		Talked
	11:21 AM	Andrew Cuomo, Attorney General		Talked
	11:09 AM	John Dugan		Talked
	9:45 AM	Mario Draghi		Talked
11/13/2008	5:52 PM	Michael Nelson		Talked
	5:37 PM	Hank Paulson		Talked
	5:15 PM	Trish Mosser		Talked
	5:06 PM	Don Kohn		Talked
	1:30 PM	Lee Sachs		Talked
	12:50 PM	Lloyd Blankfein		Talked
	12:46 PM	Dr. Alan Greenspan		Talked
	12:37 PM	Congressman Michael Dunn		Talked
	12:32 PM	Pete Pettersen		Talked
	12:20 PM	Hank Paulson		Talked
	12:10 PM	Josh Steiner		Talked
	12:04 PM	Howard Rubenstein		Talked
	9:50 AM	Josh Steiner		Talked
11/12/2008	6:05 PM	Brian Smedley		Talked
	4:40 PM	Dan Jester		Talked
	4:29 PM	James Gibney		Talked
	4:27 PM	Gary Stern		Talked
	4:11 PM	Michele Smith		Talked
	2:54 PM	Stanley Fischer		Talked
	2:05 PM	Bob Hoyt		Talked
	12:52 PM	Bob Rubin		Talked
				Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	12:43 PM	Hank Greenberg	[redacted]	Talked
	12:28 PM	Nathan Sheets, Board	[redacted]	Talked
	12:24 PM	Michele Smith	[redacted]	Talked
	12:07 PM	Calvin Mitchell	[redacted]	Talked
	11:30 AM	Ralph Schlosstein	[redacted]	Talked
	10:50 AM	Chairman Bernanke	[redacted]	Talked
	9:36 AM	Josh Steiner	[redacted]	Talked
11/10/2008	3:21 PM	Larry Fink	[redacted]	Talked
	1:38 PM	David McCormick	[redacted]	Talked
	9:19 AM	David McCormick	[redacted]	Talked
	9:15 AM	Michele Smith	[redacted]	Talked
11/7/2008	6:05 PM	Hank Paulson	[redacted]	Talked
	5:45 PM	Hank Paulson	[redacted]	Talked
	3:47 PM	Michele Smith	[redacted]	Talked
	3:38 PM	Roger Ferguson	[redacted]	Talked
	3:30 PM	Bob Hoyt	[redacted]	Talked
	2:33 PM	Meg McConnell	[redacted]	Talked
	1:37 PM	Bill Dudley	[redacted]	Talked
	12:58 PM	Michael Held	[redacted]	Talked
	12:52 PM	Michele Smith	[redacted]	Talked
	11:19 AM	Hank Paulson	[redacted]	Talked
	10:35 PM	Bob Hoyt	[redacted]	Talked
	10:20 AM	Don Kohn	[redacted]	Talked
	10:17 AM	Theo Lubke	[redacted]	Talked
	10:06 AM	Michele Smith	[redacted]	Talked
	8:08 AM	Steve Friedman	[redacted]	Talked
11/6/2008	6:38 PM	Mohamed El Erian	[redacted]	Talked
	6:03 PM	David McCormick	[redacted]	Talked
	5:27 PM	Hank Paulson	[redacted]	Talked
	5:06 PM	Steve Friedman	[redacted]	Talked
	3:27 PM	Alan Batkin	[redacted]	Talked
	3:10 PM	Mario Draghi	[redacted]	Talked
	3:07 PM	Hank Paulson	[redacted]	Talked
	3:02 PM	Tim Collins	[redacted]	Talked
	2:57 PM	Paul Calello	[redacted]	Talked
	2:52 PM	Dan Jester	[redacted]	Talked
	1:06 PM	Hank Paulson	[redacted]	Talked
	1:00 PM	Christine Varney (Mike Froman's Office)	[redacted]	Talked
	11:45 AM	Michelle Smith	[redacted]	Talked
	9:38 AM	Michael Froman, Citigroup	[redacted]	Talked
11/5/2008	6:21PM	Larry Summer	[redacted]	Talked

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TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	6:10PM	Josh Steiner	[redacted]	Talked
	4:38PM	Hank Paulson		Talked
	4:25PM	Hank Paulson		Talked
	4:19PM	Lloyd Blankfein		Talked
	4:07PM	Chairman Bernanke		Talked
	4:00PM	Hank Paulson		Talked
	3:02PM	Jim Wilkinson		Talked
	1:53PM	Steve Shafran		Talked
	1:50PM	Michelle Smith		Talked
	1:44PM	Vice Chairman Kohn		Talked
	1:28PM	John Thain		Talked
	1:17PM	May Lee		Talked
	12:48PM	Lee Sachs		Talked
	9:06 AM	Michael Froman, Citigroup		Talked
	8:31 AM	Secretary Paulson		Talked
11/4/2008	6:33 PM	Secretary Paulson		Talked
	5:51 PM	Michael Froman, Citigroup		Talked
	4:03 PM	Larry Summers		Talked
	2:22 PM	Michele Smith		Talked
	1:41 PM	Chairman Bernanke		Talked
	1:29 PM	Mohamed El Erian		Talked
	1:07 PM	Arminio Fraga		Talked
	12:47 PM	Bob Rubin		Talked
	12:12 PM	Chairman Bernanke		Talked
	11:48 AM	Secretary Paulson		Talked
	11:35 AM	David Wilcox		Talked
	11:16 AM	David Viniar		Talked
	11:04 AM	Dan Jester		Talked
	10:36 AM	Chairman Bernanke		Talked
	10:30 AM	Lee Sachs		Talked
	9:48 AM	Josh Steiner		Talked
	8:42 AM	Chairman Bernanke		Talked
	8:24 AM	Lee Sachs		Talked
11/3/2008	7:20 PM?	Meg McConnell		Talked
	7:02 PM	Meg McConnell		Talked
	6:50 PM	Josh Steiner		Talked
	5:25 PM	Hank Greenberg		Talked
	5:17 PM	Jamie Dimon		Talked
	4:24 PM	Jamie Dimon		Talked
	3:47 PM	Larry Fink		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	2:18 PM	Michele Smith	[redacted]	Talked
	1:47 PM	Lee Sachs		Talked
	12:36 PM	Amy Brelia		Talked
	12:15 PM	Ben Bernanke		Talked
	11:54 AM	David Viniar		Talked
	11:27 AM	Theo Lubke		Talked
	10:55 AM	Bob Rubin		Talked
	10:50 AM	Theo Lubke		Talked
	10:49 AM	Tony Ryan		Talked
	8:36 AM	Hank Paulson		Talked
	8:30 AM	Hank Paulson		Talked
	7:50 AM	Dan Jester & David Nason		Talked
				Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
10/31/2008	5:42 PM	Ken Wilson (Treas.)	[redacted]	Talked
	4:59 PM	Dan Jester		Talked
	2:40 PM	Lee Sachs		Talked
	2:32 PM	Hank Paulson		Talked
	2:24 PM	John Dugan		Talked
	2:20 PM	Calvin Mitchell		Talked
	12:18 PM	Steve Pearlstein, Wash Post		Talked
	12:03 PM	David Oddsson, Bank of Iceland		Talked
	11:06 AM	Don Kohn		Talked
	10:55 AM	Eric Mindich		Talked
	10:20 AM	Dan Jester		Talked
	9:56 AM	Vikram Pandit		Talked
	8:58 AM	Ben Bernanke		Talked
	8:46 AM	Dan Jester		Talked
10/30/2008	7:53 PM	Sarah Dahlgren		Talked
	6:53 PM	Larry Summers		Talked
	6:30 PM	Senator Grassley		Talked
	4:21 PM	Rodgin Cohen		Talked
	4:05 PM	Hank Paulson		Talked
	1:40 PM	Ben Bernanke		Talked
	1:30 PM	Tony Ryan		Talked
	1:26 PM	Dan Jester		Talked
	1:22 PM	Dan Jester		Talked
	1:15 PM?	Hank Paulson		Talked
	12:34 PM	Kevin Warsh		Talked
	12:23 PM	Tom Nides		Talked
	12:20 PM	David Wilcox		Talked
	12:07 PM	Steve Friedman		Talked
	11:25 AM	Ben Bernanke		Talked
	11:18 AM	Tim Collins		Talked
	10:00 AM	Theo Lubke		Talked
	9:42 AM	Calvin Mitchell		Talked
	9:30 AM	David Wilcox		Talked
	8:17 AM	Dan Jester		Talked
10/29/2008	6:05 PM	Clay Lowery, Treasury		Talked
	5:59 PM	Michelle Smith		Talked
	5:31 PM	Larry Summers		Talked
	3:30 PM	Meg McConnell		Talked
	2:02 PM	Meg McConnell		Talked
	1:55 PM	Hank Paulson		Talked
10/28/2008	10:00 AM	Prime Minister Gordon Brown (UK)		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	9:02 AM	Meg McConnell	[redacted]	Talked
	8:54 AM	Sarah Dahlgren	[redacted]	Talked
10/27/2008	6:02 PM	Meg McConnell	[redacted]	Talked
	5:44 PM	Secretary Paulson	[redacted]	Talked
	4:45 PM	Larry Fink	[redacted]	Talked
	4:42 PM	Ed Liddy	[redacted]	Talked
	3:54 PM	Charles Schwab	[redacted]	Talked
	12:23 PM	John Sexton	[redacted]	Talked
	12:12 PM	Meg McConnell	[redacted]	Talked
	12:04 PM	David Wilcox	[redacted]	Talked
	11:54 AM	Robert Wilmers	[redacted]	Talked
	11:42 AM	Lloyd Blankfein	[redacted]	Talked
	10:58 AM	Dan Jester	[redacted]	Talked
	8:20 AM	Neel Kashkari, Treas.	[redacted]	Talked
10/24/2008	7:23 PM	Robert Rubin	[redacted]	Talked
Rose		Ben Bernanke	[redacted]	Talked
re-capped		Hank Paulson	[redacted]	Talked
calls for		Michelle Smith	[redacted]	Talked
this day		Reza Moghadam - IMF	[redacted]	Talked
	4:42 PM	Dan Jester	[redacted]	Talked
Log was	4:35 PM	Jim Wilkinson	[redacted]	Talked
not saved	4:03 PM	Roger Altman	[redacted]	Talked
(mw)	1:45 PM	Scott Alvarez	[redacted]	Talked
	1:33 PM	Kevin Warsh	[redacted]	Talked
		Jean Pierre Roth	[redacted]	Talked
	11:07 AM	Sandy Krieger	[redacted]	Talked
	10:20 AM	Josh Steiner	[redacted]	Talked
	10:13 AM	Bill Dudley	[redacted]	Talked
	9:56 AM	David McCormack	[redacted]	Talked
	9:29 AM	Michelle Smith	[redacted]	Talked
	9:20 AM	Don Kohn	[redacted]	Talked
	8:50 AM	Ben Bernanke	[redacted]	Talked
10/23/2008	6:38 PM	Chairman Bernanke	[redacted]	Talked
	5:29 PM	Larry Summers	[redacted]	Talked
	3:43 PM	Jean Pierre Roth	[redacted]	Talked
	3:16 PM	Dan Jester	[redacted]	Talked
	3:15 PM	Dan Jester	[redacted]	Talked
	2:50 PM ?	Chairman Bernanke	[redacted]	Talked
	1:35 PM	Jeff Lacker	[redacted]	Talked
	1:03 PM	Don Kohn	[redacted]	Talked
	12:40 PM	Scott Alvarez	[redacted]	Talked
			[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
		Bob Kelly	[redacted]	
	10:40 AM	Jamie Dimon		Talked
	10:27 AM	Steve Shafran		Talked
	10:14 AM	Robert Wilmers		Talked
	10:03 AM	Senator Charles Schumer		Talked
	9:55 AM	Lloyd Blankfein		Talked
	8:47 AM	Chairman Bernanke		Talked
	8:30 AM	Jean-Claude Trichet		Talked
10/22/2008	6:31 PM	Larry Fink		Talked
	6:25 PM	Secretary Paulson		Talked
	6:22 PM	Rodgin Cohen		Talked
	6:14 PM	Secretary Paulson		Talked
	5:10 PM	David Nason		Talked
	5:03 PM	Scott Alvarez		Talked
	1:40 PM	Art Murton, FDIC		Talked
	11:06 AM	Robert Wilmers		Talked
	11:00 AM	Rodgin Cohen		Talked
	10:22 AM	Nathan Sheets, Board		Talked
10/21/2008	6:16 PM	Calvin Mitchell		Talked
	6:00 PM	Larry Fink		Talked
	5:30 PM	John Dugan		Talked
	5:13 PM	Lewis Alexander		Talked
	3:56 PM	Gov Meirelles, Cntrl Bank of Brazil		Talked
	1:45 PM	John Mack		Talked
	12:58 PM	Lloyd Blankfein		Talked
	1:03 PM	Lee Sachs		Talked
	12:27 PM	Dan Jester		Talked
	12:12 PM	Gene Sperling		Talked
	11:59 AM	Vikram Pandit		Talked
	11:53 AM	Jeff Immelt		Talked
	11:49 AM	Calvin Mitchell		Talked
	10:50 AM	Michele Smith		Talked
	10:33 AM	John Dugan		Talked
	10:13 AM	Chairman Bernanke		Talked
	9:47 AM	Gene Sperling		Talked
	9:46 AM	Doug Elmendorf		Talked
	9:39 AM	David Dreyer		Talked
	9:19 AM	David Wilcox		Talked
	8:33 AM	Secretary Paulson		Talked
10/20/2008	6:20 PM ?	Don Kohn and Kevin Warsh		Talked
	6:09 PM	Lee Sachs		Talked
	6:04 PM	Edward Liddy		Talked
				Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	5:28 PM	Lloyd Blankfein	[redacted]	Talked
	5:02 PM	Dan Jester		Talked
	5:00 PM	Calvin Mitchell		Talked
	5:55 PM	Chairman Bernanke		Talked
	4:45 PM	Dan Jester		Talked
	4:24 PM	Dan Jester and David Nason		Talked
	2:52 PM	Frank Brosens		Talked
	2:42 PM	Ken Garbade		Talked
	2:27 PM	Frank Brosens		Talked
	2:05 PM	Robert Rubin		Talked
	2:04 PM	Dan Jester		Talked
	1:45 PM	Sheryl Sandberg		Talked
	1:10 PM	Josh Steiner		Talked
	1:07 PM	Secretary Paulson		Talked
	1:05 PM	Josh Steiner		Talked
	1:00 PM	Jamie Dimon		Talked
	12:15 PM	Paul Tudor Jones		Talked
	9:41 AM	Kevin Warsh		Talked
	9:22 AM	Ralph Schlosstein		Talked
	9:10 AM	David Nason		Talked
	9:02 AM	Oliver Pawle, Partner, Whitehead Mann Partnership		Talked
	8:38 AM	Secretary Paulson		Talked
	8:37 AM	Secretary Paulson		Talked
10/17/2008	5:55 PM	Jeremy Stein		Talked
	5:40 PM	Josh Steiner		Tim called on cell
	5:33 PM	Michele Smith		Talked
	5:17 PM	Larry Summers		Talked
	5:11 PM	Jeff Immelt		Talked
	4:51 PM	Tim Collins		Talked
	4:47 PM	Calvin Mitchell		Talked
	4:36 PM	Secretary Paulson		Talked
	3:13 PM	Walt Lukken		Talked
	3:08 PM	Steve Friedman		Talked
	12:25 PM	Kevin Warsh		Talked
	12:02 PM	David Nason		Talked
	11:52 AM	Congressman Paul Ryan (608-752-4050 office)		Talked
	11:01 AM	Chairman Bernanke		Talked
	10:47 AM	Ken Wilson (Treas.)		Talked
	10:41 AM	Hildebrand		Talked
	10:37 AM	Secretary Paulson		Talked
	9:17 AM	Chairman Bernanke		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	9:03 AM	Michael Froman, Citigroup	[redacted]	Talked
10/16/2008	7:02 PM	Robert Rubin		Talked
	6:25 PM	Larry Summers		Talked
	6:15 PM	Secretary Paulson		Talked
	5:26 PM	Lally Weymouth		Talked
	5:12 PM	John Rich, OTS		Talked
	4:22 PM	Don Kohn		Talked
	4:20 PM	Lee Sachs		Talked
	4:06 PM	Andrew Cuomo		Talked
	3:54 PM	Andrew Cuomo		Talked
	3:33 PM	John Thain		Talked
	3:31 PM	Andrew Cuomo		Talked
	3:28 PM	Secretary Paulson		Talked
	3:21 PM	Randy Kroszner		Talked
	3:04 PM	~~Bob Diamond~~ Mr. Ricci? Took the call for Bob		Talked
	2:11 PM	Bob Diamond		Talked
	1:58 PM	Jerry Corrigan		Talked
	1:39 PM	John Dugan		Talked
	12:25 PM	Daniel Heller, Swiss Nat'l Bank		Talked
	9:24 AM	Andrew Cuomo		Talked
	9:16 AM	Secretary Paulson		Talked
	9:12 AM	Rodgin Cohen		Talked
	7:24 AM	Sarah Dahlgren		Talked
10/15/2008	--	Paul Catello		Check [illegible] to return call
	--	Jamie Dimon		Talked as per TFG
	--	Larry Summers		Talked as per TFG
	6:25 PM	Lee Sachs		Talked
	6:15 PM	Larry Fink		Talked
	5:50 PM	Secretary Paulson		Talked
	5:46 PM	John Hogan		Talked
	5:45 PM	Calvin Mitchell		Talked
	4:08 PM	Dan Jester		Talked
	4:32 PM	Ken Chenault, American Express		Talked
	3:49 PM	Jamie Dimon		Talked
	2:52 PM	Josh Steiner		Talked
	2:50 PM	Secretary Paulson		Talked
	2:33 PM	Lewis Kaden		Talked
	11:38 AM	Meg		Talked
	11:30 AM	Mike Alix		Talked
	11:09 AM	Steve Liesman, CNBC		Talked
	10:20 AM	Stanley Fischer		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	9:42 AM	Kevin Warsh	[redacted]	Talked
	9:36 AM	Michael Froman, Citigroup		Talked
	8:54 AM	Michelle Smith		Talked
	8:32 AM	John Dugan		Talked
	8:30 AM	Lewis Kaden		Talked
	8:16 AM	Jeff Lacker		Talked
10/14/2008	6:53 PM	Senator Schumer		Talked
	6:04 PM	Mike Alix		Talked
	5:44 PM	Josh Steiner		Talked
	5:20 PM	Dan Doctoroff		Talked
	2:53 PM	Larry Fink		Talked
	2:50 PM	Mohamed El Erian		Talked
	2:44 PM	Ken Lewis - Bnk or Amr		Talked
	12:37 PM	Michael "Mickey" Kantor (Former Secy of Commerce)		Talked
	12:29 PM	Don Kohn		Talked
	12:16 PM	Rodgin Cohen		Talked
	12:08 PM	Theo Lubke		Talked
	10:30 AM	Robert Wilmers		Talked
	10:04 AM	Steve Friedman		Talked
	9:49 AM	Lee Sachs		Talked
	9:40 AM	Rahm Emanuel		Talked
	9:30 AM	Sarah Dahlgren		Talked
	6:11 PM	Scott Alvarez		Talked
10/13/2008	6:54 PM	Jeff Immelt		Talked
	6:11 PM	Scott Alvarez		Talked
	6:03 PM	Don Kohn		Talked
	5:56 PM	Rodgin Cohen		Talked
	5:54 PM	Don Kohn		Talked
	9:20 AM	Bill Dudley		Talked
	9:11 AM	Michael Silva		Talked
	9:01 AM	Tom Nides		Talked
	8:56 AM	Chairman Bernanke		Talked
	8:42 AM	Jamie Dimon		Talked
	8:25 AM	Calvin Mitchell		Talked
12/12/2008	12:15 PM	Bob Diamond		Talked
10/10/2008	6:57 PM	Chairman Bernanke		Talked
	6:49 PM	Sarah Dahlgren		Talked
	6:44 PM	Lloyd Blankfein		Talked
	6:42 PM	Jamie Dimon		Talked
	6:36 PM	Larry Fink		Talked
	7:24 PM	Secretary Paulson		Talked

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REDACTED

TALK SHEET

Talked

DATE	TIME	CALLER	PHONE #	MESSAGE
	7:19 PM	Bill Dudley	[redacted]	Talked
	6:10 PM	Kevin Warsh	[redacted]	Talked
	5:29 PM	Christal (Paulson's assistant)	[redacted]	Talked
	4:04 PM	Michele Smith	[redacted]	Talked
	3:22 PM	Sheila Bair	[redacted]	Talked
	1:43 PM	David McCormick	[redacted]	Talked
	1:42 PM	David McCormick	[redacted]	Talked
	12:35 PM	Senator Charles Schumer	[redacted]	Talked
	12:32 PM	JeanMarie Davis	[redacted]	Talked
	12:22 PM	Michelle Smith	[redacted]	Talked
	12:17 PM	Sandy Krieger	[redacted]	Talked
	11:55 AM	Chairman Bernanke	[redacted]	Talked
	11:54 AM	David McCormick	[redacted]	Talked
	11:30 AM	Alan Greenspan	[redacted]	Talked
	11:29 AM	Dan Doctoroff	[redacted]	Talked
	11:19 AM	Jamie Dimon	[redacted]	Talked
	11:17 AM	David Viniar	[redacted]	Talked
	10:43 AM	Dan Jester	[redacted]	Talked
	10:17 AM	Tom Nides	[redacted]	Talked
	10:04 AM	Secretary Paulson	[redacted]	Talked
	9:39 AM	Don Kohn	[redacted]	Talked
	9:35 AM	David McCormick	[redacted]	Talked
	9:32 AM	Michelle Smith	[redacted]	Talked
	9:29 AM	Chairman Bernanke	[redacted]	Talked
	9:26 AM	Secretary Paulson	[redacted]	Talked
	9:20 AM	Sheila Bair	[redacted]	Talked
	9:17 AM	Michelle Smith	[redacted]	Talked
	9:09 AM	Chairman Bernanke	[redacted]	Talked
	8:38 AM	Secretary Paulson	[redacted]	Talked
	8:26 AM	Dan Jester	[redacted]	Talked
	8:18 AM	Rodgin Cohen	[redacted]	Talked
10/9/2008	6:39 PM	Bob Greifeld, NASDAC	[redacted]	Talked
	6:36 PM	Robert Rubin	[redacted]	Talked
	6:28 PM	Secretary Paulson	[redacted]	Talked
	6:06 PM	Ned Kelly	[redacted]	Talked
	6:05 PM	Jamie Dimon	[redacted]	Talked
	5:17 PM	John Thain	[redacted]	Talked
	4:50 PM	Tom Nides	[redacted]	Talked
	4:47 PM	Chairman Bernanke	[redacted]	Talked
	4:40 PM	Jean-Claude Trichet	[redacted]	Talked
	3:55 PM	Ken Wilson (Treas.)	[redacted]	Talked

REDACTED

TALK SHEET

Talked

DATE	TIME	CALLER	PHONE #	MESSAGE
	3:51 PM	Secretary Paulson	[redacted]	Talked
	3:45 PM	Ken Wilson (Treas.)	[redacted]	Talked
	3:40 PM	Secretary Paulson	[redacted]	Talked
	3:10 PM	Kevin Warsh	[redacted]	Talked
	1:30 PM	Larry Summers	[redacted]	Talked
	1:20 PM	Michael Held	[redacted]	Talked
	1:00 PM	Secretary Paulson	[redacted]	Talked
	12:57 PM	Bob Diamond, Barclays	[redacted]	Talked
	12:53 PM	Vikram Pandit	[redacted]	Talked
	12:23 PM	Steve Friedman	[redacted]	Talked
	12:11 PM	Vikram Pandit	[redacted]	Talked
			[redacted]	Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	12:06 PM	Tom Nides	[redacted]	Talked
	11:15 AM	Dan Jester	[redacted]	Talked
	11:11 AM	Dan Jester	[redacted]	Talked
	10:51 AM	Paul Volcker	[redacted]	Talked
	10:47 AM	Stan Druckenmiller	[redacted]	Talked
	10:30 AM	Dan Jester	[redacted]	Talked
	10:18 AM	Secretary Paulson	[redacted]	Talked
	9:52 AM	Kevin Warsh	[redacted]	Talked
	9:50 AM	Charles Wait	[redacted]	Talked
	9:43 AM	Steve Friedman	[redacted]	Talked
	9:39 AM	Michael Held	[redacted]	Talked
	9:38 AM	JeanMarie Davis	[redacted]	Talked
	9:32 AM	Ken DeRegt	[redacted]	Talked
	9:29 AM	Jamie Dimon	[redacted]	Talked
	9:15 AM	Don Kohn	[redacted]	Talked
	9:00 AM	Chairman Bernanke	[redacted]	Talked
	8:28 AM	Don Kohn	[redacted]	Talked
	Time unknown - TFG Advised	Dan Jester	[redacted]	Talked
	Time unknown - TFG Advised	Secretary Paulson	[redacted]	Talked
	Time unknown - TFG Advised	Secretary Paulson	[redacted]	Talked
10/8/2008	7:15 PM	Dan Jester	[redacted]	Talked
	7:01 PM	Lee Sachs	[redacted]	Talked
	6:29 PM	Meg McConnell	[redacted]	Talked
	4:40 PM	Don Kohn	[redacted]	Talked
	4:35 PM	Secretary Paulson	[redacted]	Talked
	4:30 PM	Don Kohn	[redacted]	Talked
	3:55 PM	Mayor Bloomberg	[redacted]	Talked
	3:50 PM	Rahm Emanuel	[redacted]	Talked
	3:44 PM	John Dugan	[redacted]	Talked
	3:31 PM	Steve Friedman	[redacted]	Talked
	3:00 PM	Jerry Corrigan	[redacted]	Talked
	2:58 PM	Jamie Dimon	[redacted]	Talked
	2:52 PM	Checki	[redacted]	Talked
	2:48 PM	Secretary Paulson	[redacted]	Talked
	2:45 PM	Michelle Smith	[redacted]	Talked
	2:43 PM	Secretary Paulson	[redacted]	Talked
	2:40 PM	Michelle Smith	[redacted]	Talked
	2:39 PM	Larry Summers	[redacted]	Talked
	2:24 PM	Chairman Bernanke	[redacted]	Talked
	2:24 PM	David Viniar	[redacted]	Talked
	2:20 PM	Jamie Dimon	[redacted]	Talked

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REDACTED

TALK SHEET

Talked

DATE	TIME	CALLER	PHONE #	MESSAGE
	2:19 PM	Sandy Krieger	[redacted]	Talked
	2:16 PM	Michelle Smith		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	2:09 PM	Chairman Bernanke	[redacted]	Talked
	2:00 PM	Chairman Bernanke	[redacted]	Talked
	1:48 PM	Jamie Dimon	[redacted]	Talked
	1:45 PM	Secretary Paulson	[redacted]	Talked
	1:27 PM	Don Kohn	[redacted]	Talked
		David Stileman, Standard Chartered	[redacted]	Rulledge
	1:19 PM	Ned Kelly	[redacted]	Talked
	12:36 PM	Chairman Bernanke and Secretary Paulson	[redacted]	Talked
	12:30 PM	John Dugan	[redacted]	Talked
	12:21 PM	Secretary Paulson	[redacted]	Talked
	11:55 AM	Chairman Bernanke	[redacted]	Talked
	11:54 AM	Ned Kelly	[redacted]	Talked
	10:52 AM	Secretary Paulson	[redacted]	Talked
	10:47 AM	Kevin Warsh	[redacted]	Talked
	10:45 AM	Don Kohn	[redacted]	Talked
	10:33 AM	Vikram Pandit	[redacted]	Talked
	10:30 AM	Bob Hoyt	[redacted]	Talked
	10:24 AM	Kevin Warsh	[redacted]	Talked
	10:16 PM	Secretary Paulson	[redacted]	Talked
	10:01 AM	David McCormick	[redacted]	Talked
	9:22 AM	Secretary Paulson	[redacted]	Talked
	9:12 AM	Kevin Warsh	[redacted]	Talked
	9:07 AM	Vikram Pandit	[redacted]	Talked
	8:51 AM	Pat Parkinson	[redacted]	Talked
	8:45 AM	Secretary Paulson	[redacted]	Talked
	8:39 AM	David McCormick	[redacted]	Talked
	8:26 AM	Kevin Warsh	[redacted]	Talked
	8:01 AM	Secretary Paulson	[redacted]	Talked
	7:45 AM	Secretary Paulson	[redacted]	Talked
10/7/2008	7:05 PM	Jamie Dimon	[redacted]	Talked
	6:57 PM	Bill Lockyer, Calif State Treasurer	[redacted]	Talked
	6:53 PM	Jeff Immelt	[redacted]	Talked
	6:48 PM	Larry Fink	[redacted]	Talked
	6:46 PM	Dave McCormick	[redacted]	Talked
	5:22 PM	John Thain	[redacted]	Talked
	5:17 PM	Gary Parr	[redacted]	Talked
	5:08 PM	Secretary Paulson	[redacted]	Talked
	5:03 PM	Secretary Paulson	[redacted]	Talked
	5:01 PM	Ken Wilson (Treas.)	[redacted]	Talked
	4:54 PM	Labe Jackson, on Bd of JP Morgan	[redacted]	Talked
	3:56 PM	John Dugan	[redacted]	Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	3:52 PM	Kevin Warsh	[redacted]	Talked
	3:35 PM	Vikram Pandit		Talked
	3:31 PM	Tony Ryan		Talked
	3:03 PM	Jack Brennan, Vanguard		Talked
	2:55 PM	Tom Nides		Talked
	2:24 PM	Brian Madigan		Talked
	2:14 PM	Rodgin Cohen		Talked
	2:06 PM	Rodgin Cohen		Talked
	2:01 PM	John Mack		Talked
	1:58 PM	Rodgin Cohen		Talked
	1:56 PM	Dan Jester		Talked
	1:55 PM	Secretary Paulson		Talked
	1:41 PM	Secretary Paulson		Talked
	1:36 PM	Marcel Rohner		Talked
	1:32 PM	Rodgin Cohen		Talked
	1:25 PM	Lloyd Blankfein		Talked
	1:22 PM	Bill Dudley		Talked
	11:47 AM	Mayor Bloomberg		Talked
		Peter Fisher (Mr. Geithner told Terry to call)		Talked
	11:38 AM	Michelle Smith		
	11:25 AM	Don Kohn		Talked
	11:22 AM	Steve Schwarzman		Talked
	11:19 AM	Warren Buffett		Talked
	10:47 AM	Lloyd Blankfein		Talked
	10:41 AM	Larry Fink		Talked
	10:37 AM	Chairman Bernanke		Talked
	9:08 AM	Michelle Smith		Talked
	9:01 AM	Secretary Paulson		Talked
	8:59 AM	Scott Alvarez		Talked
	8:40 AM	Kevin Warsh		Talked
	8:38 AM	Chairman Bernanke		Talked
	8:26 AM	Secretary Paulson		Talked
	8:18 AM	Secretary Paulson		Talked
	8:04 AM	Bill Dudley		Talked
10/6/2008	7:31 PM	Chairman Bernanke		Talked
	6:34 PM	Jamie Dimon		Talked
	6:32 PM	Bill Dudley		Talked
	6:25 PM	Michelle Smith		Talked
	5:53 PM	Don Kohn		Talked
	5:49 PM	Secretary Paulson		Talked
	5:45 PM	Don Kohn		Talked
				Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	5:33 PM	Secretary Paulson	[redacted]	Talked
	5:32 PM	Michelle Smith	[redacted]	Talked
	5:23 PM	Jerry Corrigan	[redacted]	Talked
	5:17 PM	Michelle Smin	[redacted]	Talked
	5:12 PM	Pat Parkinson	[redacted]	Talked
	5:00 PM	Senator Richard Burr	[redacted]	Talked
	4:39 PM	Kevin Warsh	[redacted]	Talked
	4:28 PM	Chairman Bernanke	[redacted]	Talked
	4:19 PM	Secretary Paulson	[redacted]	Talked
	4:17 PM	Duncan Niederauer, CEO, NYSE	[redacted]	Talked
	4:08 PM	Jeff Immelt	[redacted]	Talked
	3:50 PM	Vikram Pandit	[redacted]	Talked
	3:44 PM	David Nason	[redacted]	Talked
	3:41 PM	Scott Alvarez	[redacted]	Talked
	3:26 PM	Michelle Smith	[redacted]	Talked
	3:22 PM	Bill Dudley	[redacted]	Talked
	3:21 PM	Michelle Smith	[redacted]	Talked
	3:14 PM	Kevin Warsh	[redacted]	Talked
	2:59 PM	Vikram Pandit	[redacted]	Talked
	2:55 PM	Secretary Paulson	[redacted]	Talked
	2:51 PM	Don Kohn	[redacted]	Talked
	2:42 PM	Chairman Bernanke	[redacted]	Talked
	2:05 PM	Christian Noyer & Axel Weber	[redacted]	Talked
	1:56 PM	Kevin Warsh	[redacted]	Talked
	1:55 PM	Meg McConnell	[redacted]	Talked
	1:35 PM	Secretary Paulson	[redacted]	Talked
	1:34 PM	Bob Greifeld, NASDAC	[redacted]	Talked
	1:29 PM	Secretary Paulson	[redacted]	Talked
	1:24 PM	Senator Charles Schumer	[redacted]	Talked
	1:01 PM	Chairman Bernanke	[redacted]	Talked
	12:50 PM	Gov. Geuillermo Ortis, Gov., Cntrl Bnk of Mexico	[redacted]	Talked
	12:27 PM	Gov. Geuillermo Ortis, Gov., Cntrl Bnk of Mexico	[redacted]	Talked
	12:20 PM	William Rhodes	[redacted]	Talked
	12:10 AM?	Chairman Bernanke	[redacted]	Talked
	11:48 AM	Secretary Paulson	[redacted]	Talked
	11:33 AM	Elizabeth (Betsy) Duke, Governor, BOG	[redacted]	Talked
	11:03 AM	Mario Draghi	[redacted]	Talked
	10:54 AM	Michelle Smith	[redacted]	Talked
	10:26 AM	Tom Nides	[redacted]	Talked
	10:16 AM	Tom Baxter	[redacted]	Talked
	10:10 AM	Dick Peach	[redacted]	Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	9:46 AM	John Thain	[redacted]	Talked
	9:43 AM	Steve Feinberg	[redacted]	Talked
	8:22 AM	Chairman Bernanke	[redacted]	Talked
	8:19 AM	Don Kohn	[redacted]	Talked
	8:12 AM	Bill Dudley	[redacted]	Talked
	8:09 AM	Lewis Kaden	[redacted]	Talked
	7:49 AM	Dan Jester	[redacted]	Talked
10/5/2008	7:22 PM	Stafford Via	[redacted]	Talked
	5:56 PM	Kevin Warsh	[redacted]	Talked
	5:22 PM	Ned Kelly	[redacted]	Talked
	5:07 PM	Dave McCormick	[redacted]	Talked
	4:23 PM	Bob Rubin	[redacted]	Talked
	4:09 PM	Michelle Smith	[redacted]	Talked
	3:37 PM	Bob Rubin	[redacted]	Talked
	3:22 PM	Dan Jester	[redacted]	Talked
	2:35 PM	Hildebrand	[redacted]	Talked
	2:49 PM	Don Kohn	[redacted]	Talked
	2:12 PM	Kevin Warsh	[redacted]	Talked
	2:08 PM	Michelle Smith	[redacted]	Talked
	2:00 PM	Don Kohn	[redacted]	Talked
	1:58 PM	Dan Jester	[redacted]	Talked
	1:46 PM	Secretary Paulson	[redacted]	Talked
	1:42 PM	Chairman Bernanke	[redacted]	Talked
	1:39 PM	Chairman Bernanke	[redacted]	Talked
	1:08 PM	President Axel Weber	[redacted]	Talked
	12:06 PM	Kevin Warsh	[redacted]	Talked
	12:05 PM	Chairman Bernanke	[redacted]	Talked
	11:57 AM	Michelle Smith	[redacted]	Talked
	11:26 AM	Dan Jester	[redacted]	Talked
	10:01 AM	Dan Jester	[redacted]	Talked
	9:14 AM	Lewis Kaden	[redacted]	Talked
10/4/2008	9:24 PM	Kevin Warsh	[redacted]	Talked
	9:09 PM	Kevin Warsh	[redacted]	Talked
	8:07 PM	Kevin Warsh	[redacted]	Talked
	7:39 PM	Ned Kelly	[redacted]	Talked
	7:01 PM	Secretary Paulson	[redacted]	Talked
	6:42 PM	Kevin Warsh	[redacted]	Talked
	5:49 PM	Lloyd Blankfein	[redacted]	Talked
	4:49 PM	Chairman Bernanke	[redacted]	Talked
	4:34 PM	Kevin Warsh	[redacted]	
	4:23 PM	Ned Kelly	[redacted]	Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	4:22 PM	David Nason	[redacted]	Talked
	4:15 PM	Kevin Warsh		Talked
	4:10 PM	Rodgin Cohen		Talked
	2:40 PM	Chairman Bernanke		Talked
	2:38 PM	Dan Jester		Talked
	1:22 PM	Secretary Paulson		Talked
	1:11 PM	Michelle Smith & Michelle Davis		Talked
	1:06 PM	Michelle Smith		Talked
	12:45 PM (approx)	Congressman Rahm Emaunel		Talked
	12:36 PM	Gary Crittenden		Talked
	12:35 PM	David Nason		Talked
	12:11 PM	Brian Leach & Gary Crittenden		Talked
	11:59 AM	Dan Jester		Talked
	11:30 AM	Secretary Paulson		Talked
	11:12 AM	Bob Rubin		Talked
10/3/2008	7:27 PM	Tom Baxter		Talked
	7:25 PM	Chairman Bernanke		Talked
	7:21 PM	Don Kohn		Talked
	7:17 PM	Tom Baxter		Talked
	7:10 PM	Secretary Paulson		Talked
	6:40 PM	Ned Kelly		Talked
	6:34 PM	Chairman Bernanke & Don Kohn		Talked
	6:30 PM	Ralph Schlosstein		Talked
	6:29 PM	Ned Kelly		Talked
	6:12 PM	Robert Rubin		Talked
	4:46 PM	Ralph Schlosstein		Talked
	4:36 PM	Chairman Bernanke		Talked
	4:25 PM	Bob Steel		Talked
	4:24 PM	Evan Brown (Markets)		Talked
	4:22 PM	Checki		Talked
	4.19 PM	Checki		Talked
	4:13 PM	Ned Kelly		Talked
	3:52 PM	Jamie Dimon		Talked
	3:42 PM	Sheila Bair		Talked
	3:21 PM	Ed Forst		Talked
	3:16 PM	David Nason		Talked
	3:08 PM	Robert Rubin		Talked
	3:02 PM	John Dugan		Talked
	--	John Snow & Steve Feinberg, CEO Cerberus		Talked
	2:32 PM	Lewis Kaden		Checki & Dudley to return call
	2:29 PM	Ned Kelly		Talked
				Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	2:26 PM	Larry Fink	[redacted]	
	1:54 PM	Secretary Paulson		Talked
	1:49 PM	David Nason		Talked
	12:57 PM	Secretary Paulson		Talked
	12:56 PM	Vikram Pandit		Talked
	12:27 PM	Ned Kelly		Talked
	12:15 PM	Sheila Bair		Talked
	12:05 PM	Vikram Pandit		Talked
	12:01 PM	John Dugan		Talked
	11:49 AM	Bob Diamond		Talked
	11:44 AM	Sheila Bair		Talked
	11:40 AM	Theo Lubke		Talked
	11:40 AM	Ed Forst		Talked
	11:38 AM	Jamie McAndrews		Talked
	11:37 AM	Secretary Paulson		Talked
	11:28 AM	Don Kohn		Talked
	11:21 AM	Chairman Bernanke		Talked
	11:02 AM	Secretary Paulson		Talked
	11:02 AM	Prof. Nouriel Roubini's Office		Talked
	10:53 AM	Michelle Smith		[illegible]
	10:45 AM	Jeff Immelt		Talked
	10:19 AM	Dan Jester		Talked
	10:08 AM	Tony Ryan & David Nason		Talked
	10:02 AM	Scott Alvarez		Talked
	9:42 AM	Chairman Bernanke		Talked
	9:37 AM	Chairman Bernanke		Talked
	9:22 AM	Secretary Paulson		Talked
	9:15 AM	Ned Kelly		Talked
	9:12 AM	Vikram Pandit		Talked
	8:58 AM	Brackett Denniston		Talked
	8:53 AM	Jamie Dimon		Talked
	8:49 AM	Ned Kelly		Talked
	8:39 AM	Sheila Bair		Talked
	8:35 AM	Scott Alvarez & V.C. Kohn		Talked
	8:33 AM	Vikram Pandit		Talked
	8:19 AM	Robert Rubin		Talked
	8:09 AM	Sheila Bair & Scott Alvarez		Talked
	8:03 AM	Scott Alvarez		Talked
	8:00 AM	Secretary Paulson		Talked
	7:57 AM	Bob Rubin		Talked
10/2/2008	8:57 PM	Dan Jester		Talked
	8:50 PM	Kevin Warsh		Talked
				Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	8:34 PM	Chairman Bernanke	[redacted]	Talked
	8:27 PM	Dan Jester	[redacted]	Talked
	8:22 PM	Kevin Warsh	[redacted]	Talked
	8:19 PM	Secretary Paulson	[redacted]	Talked
	8:05 PM	Dan Jester	[redacted]	Talked
	8:00 PM	Dan Jester	[redacted]	Talked
	7:56 PM	Kevin Warsh	[redacted]	Talked
	7:53 PM	Rodgin Cohen	[redacted]	Talked
	7:45 PM	Rodgin Cohen	[redacted]	Talked
	7:36 PM	Bob Diamond	[redacted]	Talked
	7:11 PM	Jamie Dimon	[redacted]	Talked
	7:00 PM	Dan Jester	[redacted]	Talked
	6:45 PM	Chairman Bernanke	[redacted]	Talked
	5:20 PM	Secretary Paulson	[redacted]	Talked
	4:44 PM	Richard Carrion	[redacted]	Talked
	4:15 PM apx	Ralph Schlosstein	[redacted]	Talked
	3:57 PM	John Dugan	[redacted]	Talked
	3:41 PM	Secretary Paulson	[redacted]	Talked
	3:21 PM	Don Kohn	[redacted]	Talked
	3:18 PM	Secretary Paulson	[redacted]	Talked
	3:04 PM	Secretary Paulson	[redacted]	Talked
	2:58 PM	Kevin Warsh	[redacted]	Talked
	2:54 PM	Secretary Paulson	[redacted]	Talked
	2:48 PM	Secretary Paulson	[redacted]	Talked
	2:16 PM	Steve Friedman	[redacted]	Talked
	1:26 PM	Secretary Paulson	[redacted]	Talked
	12:16 PM	Alan Greenspan	[redacted]	Talked
	11:40 AM	Alan Greenspan	[redacted]	Talked
	11:26 AM	Secretary Paulson	[redacted]	Talked
	11:00 AM	Martin Grant	[redacted]	Talked
	10:44 AM	Kevin Warsh	[redacted]	Talked
	10:42 AM	Scott Alvarez	[redacted]	Talked
	10:16 AM	Chrystia Freeland	[redacted]	Talked
	9:56 AM	Roger Altman	[redacted]	Talked
	9:29 AM	Michelle Smith	[redacted]	Talked
	9:25 AM	John Dugan	[redacted]	Talked
	9:21 AM	Bob Diamond	[redacted]	Talked
	9:18 AM	Jeff Immelt	[redacted]	Talked
	9:04 AM	Dan Jester	[redacted]	Talked
	8:57 AM	Sheila Bair	[redacted]	Talked
	8:53 AM	Don Kohn	[redacted]	Talked
	8:38 AM	Bill Dudley	[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	8:32 AM	David Oddsson, Bank of Iceland	[redacted]	Talked
	8:23 AM	Larry Summers		Talked
10/1/2008	5:22 PM	Paul Volcker		Talked
	4:53 PM	Theo Lubke		Talked
	4:27 PM	Vikram Pandit		Talked
	4:20 PM	Dan Jester		Talked
	3:59 PM	Alan Greenspan		Talked
	3:50 PM	Lloyd Blanklein		Talked
	3:41 PM	Larry Fink		Talked
	3:33 PM	Rodgin Cohen		Talked
	3:23 PM	Don Kohn		Talked
	3:20 PM	Michael Schetzel		Talked
	3:15 PM	Secretary Paulson		Talked
	3:13 PM	Rodgin Cohen		Talked
	3:09 PM	Rita Proctor		Talked
	3:04 PM	Chairman Bernanke		Talked
	2:59 PM	John Dugan		Talked
	2:50 PM	Kevin Warsh		Talked
	1:43 PM	Chairman Cox		Talked
	1:25 PM	John Dugan		Talked
	12:52 PM	Vikram Pandit & Ned Kelly		Talked
	12:32 PM	Tony Ryan		Talked
	12:14 PM	Jeff Lacker		Talked
	12:00 PM	Bill Dudley		Talked
	11:45 AM	Dan Jester		Talked
	11:43 AM	Secretary Paulson		Talked
	11:29 AM	Meg McConnell		came over
	11:17 AM	Don Kohn		Talked
	11:14 AM	Vikram Pandit		Talked
	11:10 AM	Secretary Paulson		Talked
	10:25 AM	Calvin Mitchell		Talked
	9:24 AM	Don Kohn		Talked
	9:19 AM	Ned Kelly		Talked
	9:16 AM	Secretary Paulson		Talked
	9:03 AM	Hank Greenberg		Talked
	8:39 AM	Rodgin Cohen		Talked
	8:30 AM	President Axel Weber		Talked
	7:44 AM	Ned Kelly		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
9/30/2008	7:38 PM	Don Kohn	[redacted]	Talked
	7:18 PM	David Nason	[redacted]	Talked
	7:09 PM	Lee Sachs	[redacted]	Talked
	7:01 PM	Jeff Immelt	[redacted]	Talked
	6:48 PM	Dan Jester	[redacted]	Talked
	6:41 PM	Paul Volcker	[redacted]	Talked
	5:30 PM	John Dugan	[redacted]	Talked
	3:46 PM	Larry Summers	[redacted]	Talked
	3:43 PM	Secretary Paulson	[redacted]	Talked
	3:33 PM	Dan Jester	[redacted]	Talked
	3:29 PM	Chairman Bernanke	[redacted]	Talked
	3:19 PM	Larry Summers	[redacted]	Talked
	3:17 PM	Vikram Pandit	[redacted]	Talked
	3:07 PM	John Mack	[redacted]	Talked
	3:06 PM	Jamie Dimon	[redacted]	Talked
	3:00 PM	Larry Fink	[redacted]	Talked
	2:45 PM	Alan Greenspan	[redacted]	Talked
	2:28 PM	Calvin Mitchell	[redacted]	Talked
	2:20 PM	Bill Rutledge	[redacted]	Talked
	12:54 PM	Rodgin Cohen	[redacted]	Talked
	12:21 PM	Secretary Paulson	[redacted]	Talked
	11:46 AM	Larry Summers	[redacted]	Talked
	11:26 AM	Secretary Paulson	[redacted]	Talked
	11:22 AM	Dan Jester	[redacted]	Talked
	11:08 AM	Chairman Cox	[redacted]	Talked
	11:04 AM	Bill Rutledge	[redacted]	Talked
	10:52 AM	Don Kohn	[redacted]	Talked
	10:37 AM	Jean-Claude Trichet	[redacted]	Talked
	10:20 AM	Dan Jester	[redacted]	Talked
	10:13 AM	Don Kohn	[redacted]	Talked
	9:53 AM	Chairman Bernanke	[redacted]	Talked
	9:52 AM	Rita Proctor	[redacted]	Talked
	9:14 AM	Jeff Immelt	[redacted]	Talked
	9:13 AM	Tony Ryan	[redacted]	Talked
	9:06 AM	Hank Paulson	[redacted]	Talked
	8:30 AM	Chairman Cox	[redacted]	Talked
	8:28 AM	John Dugan	[redacted]	Talked
	8:09 AM	Rita Proctor	[redacted]	Talked
	8:08 AM	Bill Dudley	[redacted]	Talked
9/29/2008	5:51 PM	Jeff Immelt	[redacted]	Talked
	5:44 PM	Jeff Immelt	[redacted]	Talked
	5:38 PM	Steve Friedman	[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	5:35 PM	Jerry Speyer	[redacted]	Talked
	5:28 PM	Hank Paulson		Talked
	4:45PM	Kevin Warsh		Talked
	4:37 PM	Rodgin Cohen		Talked
	4:23 PM	Jeff Immelt		Talked
	4:13 PM	Michele Smith		Talked
	3:35 PM	Dan Jester		Talked
	3:26 PM	Bill Rutledge		Talked
	3:19 PM	Ned Kelly		Talked
	3:18 PM	Scott Alvarez		Talked
	3:15 PM	John Dugan		Talked
	3:11 PM	Calvin Mitchell		Talked
	3:00 PM	John Dugan		Talked
	2:59 PM	Jeff Immelt		Talked
	2:55 PM	Don Kohn		Talked
	2:31 PM	Kevin Warsh		Talked
	2:16 PM	Hank Paulson		Talked
	2:13 PM	Dan Jester		Talked
	12:05 PM	Robert Rubin		Talked
	12:02 PM	Hank Paulson		Talked
	12:01 PM	Robert Rubin		Talked
	12:01 PM	Dan Jester		Talked
	11:45 AM	Ed Forster		Talked
	11:44 AM	Kevin Warsh		Talked
	11:44 AM	Ned Kelly		Talked
	11:32 AM	Ned Kelly		Talked
	11:20 AM	Meg McConnell		came over
	11:18 AM	Jean Marie Davis		can't find
	11:15 AM	Theo Lubke		came over
	11:12 AM	Kevin Warsh		we'll CB
	11:08 AM	Edward Forst		Talked
	11:02 AM	Dan Jester		Talked
	10:54 AM	John Dugan		Talked
	10:36 AM	Hank Paulson		Talked
	10:26 AM	Congressman Anthony Weiner		Talked
	10:22 AM	Bill Dudley		Talked
	8:55 AM	Steve Shafran		Talked
	8:50 AM	Pat Parkinson		Talked
	8:49 AM	Hank Paulson		Talked
	8:48 AM	Pat Parkinson		Talked
	8:40 AM	Hank Paulson		Talked
	8:03 AM	Don Kohn		Talked

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TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	8:02 AM	Michelle Smith	[redacted]	Talked
	8:00 AM	Dan Jester	[redacted]	Talked
	7:57 AM	Vikram Pandit	[redacted]	Talked
	7:50 AM	Bob Steel	[redacted]	Talked
	7:50 AM	Dan Jester	[redacted]	Talked
	7:36 AM	Jeff Lacker	[redacted]	Talked
	7:00 AM	Treasury Conference Call to reconvene @ 7:00am	[redacted]	Talked
	6:06 AM	Bob Steel	[redacted]	Talked
	5:42 AM	Bill Dudley	[redacted]	Talked
	5:38 AM	Jean Claude Trichet	[redacted]	Talked
	4:57 AM - 5:11 AM	Treasury Conference Call to reconvene @ 5:00am	[redacted]	Talked
	4:15 AM	John Dugan	[redacted]	Talked
	4:00am	C/Call w/Dugan, Ned Kelly, TFG, B. Rutledge & M. Silva	[redacted]	Talked
	3:45 AM	John Dugan	[redacted]	Talked
	3:44 AM	Chairman Bernanke	[redacted]	Talked
	3:12 AM - 3:44 AM	Treasury Conference Call	[redacted]	Talked
	2:52 AM	Chairman Bernanke, S. Alvarez & D. Kohn	[redacted]	Talked
	1:51AM - 2:51 AM	Treasury Conference Call	[redacted]	Talked
	1:47 AM	Don Kohn	[redacted]	Talked
	1:34 AM	John Dugan	[redacted]	Talked
	12:50 AM	Don Kohn	[redacted]	Talked
	12:26 AM	Chairman Bernanke	[redacted]	Talked
	12:03 AM	Chairman Bernanke	[redacted]	Talked
9/28/2008	11:16 PM	John Dugan	[redacted]	Talked
	11:08 PM	Dan Jester	[redacted]	Talked
	10:52 PM	Dan Jester	[redacted]	Talked
	10:45 PM	Kevin Warsh	[redacted]	Talked
	10:34 PM	John Dugan	[redacted]	Talked
	10:31 PM	Don Kohn	[redacted]	Talked
	10:18 PM	Dan Jester	[redacted]	Talked
	10:17 PM	Rodgin Cohen	[redacted]	Talked
	8:30 PM	Kevin Warsh	[redacted]	Talked
	8:26 PM	Dan Jester	[redacted]	Talked
	8:18 PM	Rodgin Cohen	[redacted]	Talked
	8:15 PM	Chairman Bernanke	[redacted]	Talked
	8:11 PM	John Dugan	[redacted]	Talked
	8:08 PM	Dan Jester	[redacted]	Talked
	8:00 PM	Rodgin Cohen	[redacted]	Talked
	7:58 PM	Don Kohn	[redacted]	Talked
	7:41 PM	Dan Jester & Ken Wilson	[redacted]	Talked
	7:35 PM	John Dugan	[redacted]	Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	7:32 PM	Dan Jester	[redacted]	Talked
	7:18 PM	Rodgin Cohen	[redacted]	Talked
	7:00Pm	Rodgin Cohen	[redacted]	Talked
	6:32 PM	David Nason	[redacted]	Talked
	6:22 PM	Kevin Warsh	[redacted]	Talked
	6:20 PM	John Dugan	[redacted]	Talked
	6:15 PM	Vikram Pandit	[redacted]	Talked
	6:10 PM	Dan Jester	[redacted]	Talked
	6:07 PM	Michelle Smith	[redacted]	Talked
	6:02 PM	Vikram Pandit	[redacted]	Talked
	5:46 PM	Jamie Dimon	[redacted]	Talked
	5:19 PM	Jamie Dimon	[redacted]	Talked
	5:04 PM	Dan Jester & Secretary Paulson	[redacted]	Talked
	5:01 PM	Michelle Smith	[redacted]	Talked
	4:55 PM	Dan Jester	[redacted]	Talked
	4:46 PM	Ed Liddy	[redacted]	Talked
	4:33 PM	Vikram Pandit	[redacted]	Talked
	4:18 PM	Dan Jester	[redacted]	Talked
	4:06 PM	John Dugan	[redacted]	Talked
	3:59 PM	Rodgin Cohen	[redacted]	Talked
	3:59 PM	Kevin Warsh	[redacted]	Talked
	3:51 PM	Dan Jester	[redacted]	Talked
	3:48 PM	Lloyd Blankfein	[redacted]	Talked
	3:38 PM	Michelle Smith	[redacted]	Talked
	3:28 PM	Jeff Lacker	[redacted]	Talked
	3:20 PM	Janet Yellen	[redacted]	Talked
	3:01 PM	Janet Yellen	[redacted]	Talked
	2:55 PM	John Dugan	[redacted]	Talked
	2:36 PM	Rodgin Cohen (As per TFG; Baxter will return this call)	[redacted]	Baxter (talked)
	2:34 PM	Dan Jester	[redacted]	Talked
	2:30 PM	Chairman Bernanke	[redacted]	Talked
	2:28 PM	Jeff Immelt	[redacted]	Talked
	2:08 PM	Dan Jester	[redacted]	Talked
	1:28 PM	Tom Nides	[redacted]	Talked
	1:26 PM	Rahm Emanuel (call on TFG's cell phone)	[redacted]	Talked
	1:15 PM	Dan Jester	[redacted]	Talked
	12:52 PM	Dan Jester & Treasury Team	[redacted]	Talked
	12:35 PM	Kevin Warsh	[redacted]	Talked
	12:08 PM	David Viniar	[redacted]	Talked
	12:04 PM	Don Kohn	[redacted]	Talked
	11:55 AM	Tom Baxter	[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	11:16 AM	David Viniar	[redacted]	Talked
	11:13 AM	Jeff Immelt		Talked
	11:10 AM	Bob Rubin		Talked
	10:51 AM	Tom Nides		Talked
	10:44 AM	Rodgin Cohen		Talked
	10:39 AM	Kevin Warsh		Talked
	10:18 AM	Baxter & Alvarez		Talked
	9:45 AM	David Viniar		Talked
	9:43 AM	Calvin Mitchell		Talked
	9:40 AM	Dan Jester		Talked
	9:35 AM	Lloyd Blankfein		Talked
	9:10 AM	Jamie Dimon		Talked
	8:56 AM	Lloyd Blankfein		Talked
	8:46 AM	Dan Jester		Talked
	8:31 AM	Vikram Pandit		Talked
9/27/2008				
	6:15 PM	Meg Mcconnell & Simon Potter		Talked
	6:09 PM	Dan Jester		Talked
	5:50 PM	Vikram Pandit		Talked
	5:45 PM	Larry Summers		Talked
	5:26 PM	Don Kohn		Talked
	5:18 PM	John Havens for Vikram Pandit		Talked
	5:15 PM	Secretary Paulson		Talked
	5:08 PM	Dan Jester		Talked
	4:58 PM ?	Steve Shafran		Talked
	4:21 PM	Steve Friedman		Talked
	4:08 PM	Sheila Bair		Talked
	3:41 PM	Chairman Bernanke		Talked
	3:50 PM	Vikram Pandit		Talked
	3:17 PM	Dan Jester		Talked
	3:04 PM	Kevin Warsh		Talked
	2:53 PM	Josh Steiner		Talked
	2:50 PM	Dan Jester		Talked
	2:01 PM	Kevin Warsh		Talked
	1:52 PM	Dan Jester		Talked
	1:41 PM	David Wilcox		Talked
	1:27 PM	Meg Mcconnell		Talked
	12:35 PM	Jeff Lacker		Talked
	12:03 PM	Larry Fink		Talked
	11:53 AM	Ed Forst		Talked
	11:47 AM	Secretary Paulson		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	11:43 AM	David Nason	[redacted]	Talked
	11:36 AM	Chairman Bernanke		Talked
	11:31 AM	Dan Jester and Ken Wilson		Talked
	??	Rodgin Cohen *(Tom Baxer will call)*		Baxter
	8:54 AM	Tom Nides		Talked
	8:38 AM	Jeff Jacker		Talked
9/26/2008	7:36 PM	Larry Summers		Talked
	7:17 PM	Dan Jester		Talked
	7:14 PM	Tom Nides		Talked
	6:54 PM	Lloyd Blankfein		Talked
	6:50 PM	Kevin Warsh		Talked
	6:45 PM	David Nason		Talked
	6:42 PM	Steve Shafran		Talked
	6:21 PM	Secretary Paulson		Talked
	6:07 PM	Lewis Kaden		Talked
	5:22 PM	Rodgin Cohen		Talked
	5:19 PM	Tom Nides		Talked
	5:00 PM	Kyoto Omori, Deputy Pres. Mitsubishi		Talked
	4:54 PM	Rodgin Cohen		Talked
	4:28 PM	John Dugan		Talked
	3:57 PM	Bob Rubin		Talked
	3:55 PM	Secretary Paulson		Talked
	3:49 PM	Alan Greenspan		Talked
	3:46 PM	Theo Lubke		Talked
	3:36 PM	Dan Jester		Talked
	2:40 PM	Alan Greenspan		Talked
	2:09 PM	Jerry Corrigan		Talked
	1:53 PM	Jamie Dimon		Talked
	1:49 PM	Tom Nides		Talked
	1:45 PM	Bill Dudley		Talked
	1:44 PM	Secretary Paulson		Talked
	1:40 PM	Rodgin Cohen		Talked
	12:44 PM	Jeff Immelt		Talked
	12:35 PM	Lee Sachs		Talked
	10:52 AM	Richard Haass, CFR		Talked
	10:47 AM	Vikram Pandit		Talked
	10:21 AM	Don Kohn		Talked
	10:10 AM	Dan Jester		Talked
	10:01 AM	Chairman Bernanke		Talked
	9:10 AM (approx.)	Mervyn King, BOE		Talked
	8:38 AM	Kevin Warsh		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	8:24 AM	Bill Dudley	[redacted]	
	7:46 AM	Chairman Bernanke		Talked
	7:43 AM	Dan Jester		Talked
	7:33 AM	Secretary Paulson		Talked
9/25/2008	7:41 PM	Michelle Smith		Talked
	7:25 PM	Dan Jester		Talked
	7:18 PM	Lee Sachs		Talked
	7:15 PM	Rodgin Cohen		Talked
	7:11 PM	Kevin Warsh		Talked
	6:36 PM	Chairman Bernanke		Talked
	6:32 PM	Theo Lubke		Talked
	5:58 PM	David Wilcox		Talked
	5:47 PM	Secretary Paulson		Talked
	5:33 PM	David Wilcox		Talked
	5:22 PM	Dan Jester		Talked
	4:35 PM	Vice Chairman Kohn		Talked
	4:00 PM	Kevin Warsh		Talked
	2:55 PM	Checki		Talked
	2:38 PM	Steve Pearlstein, Wash Post		Talked
	2:20 PM	Bill Rutledge		Talked
	2:17 PM	Secretary Paulson		Talked
	2:13 PM	Vice Chairman Kohn		Talked
	2:06 PM	Senator Charles Schumer		Talked
	1:56 PM	David Oddsson, Bank of Iceland		Talked
	1:50 PM	Dan Jester		Talked
	1:36 PM	Tom Nides		Talked
	1:23 PM	Bob Rubin		Talked
	1:06 PM	Vice Chairman Kohn		Talked
	12:53 PM	Rodgen Cohen		Talked
	12:34 PM	Lloyd Blankfein		Talked
	12:32 PM	Secretary Paulson		Talked
	12:26 PM	Jamie Dimon		Talked
	12:17 PM	Secretary Paulson		Talked
	12:13 PM	Senator Baucus		Talked
	12:03 PM	Dan Jester		Talked
	12:02 PM	Jean Claude Trichet		Talked
	12:00 noon	Bill Dudley		Talked
	11:54 AM	Jean Claude Trichet		Talked
	11:48 AM	Kevin Warsh		Talked
	11:35 AM	Kevin Warsh		Talked
	11:25 AM	Secretary Paulson		Talked
	11:05 AM	Ed Forst		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	10:30 AM	Chairman Bernanke, Conf Call	[redacted]	Talked
	10:28 AM	Tony Ryan & Ed Forst		Talked
	10:25 AM	Dan Jester		Talked
	10:18 AM	Chairman Bernanke		Talked
	9:21 AM	Ed Forst		Talked
	8:20 AM	David Wilcox		Talked
9/24/2008	6:28 PM	Tom Baxter		Talked
	5:53 PM	Vice Chair Kohn		Talked
	5:31 PM	Dan Jester		Talked
	5:20 PM	Rodgin Cohen (w/Mr. Hassell)		Talked
	5:15 PM	Art Angulo		Talked
	5:08 PM	Bill Dudley		Talked
	2:29 PM	John Thain		Talked
	2:09 PM	Calvin Mitchell		Talked
	1:59 PM	Kevin Warsh		Talked
	1:55 PM	Vice Chair Kohn		Talked
	1:51 PM	Larry Fink		Talked
	1:41 PM	Meg Mcconnell		Talked
	1:40 PM	John Mack		Talked
	1:23 PM	Bill Dudley		Talked
	1:18 PM	John Dugan		Talked
	1:11 PM	David Oddsson, Bank of Iceland		Talked
	1:09 PM	Rodgin Cohen		Talked
	12:58 PM	Dan Jester		Talked
	12:55 PM	Checki		Talked
	12:47 PM	Bob Rubin		Talked
	12:22 PM	Secretary Paulson		Talked
	11:59 AM	Dan Jester		Talked
	11:08 AM	Dan Jester		Talked
	10:56 AM	Roger Altman		Talked
	10:39 AM	Ed Forst		Talked
	10:26 AM	Rahm Emanuel		Talked
	10:06 AM	Dan Jester		Talked
	10:04 AM	Bill Dudley		Talked
	9:24 AM	V.C. Kohn		Talked
	8:35 AM	Larry Summers		Talked
	8:18 AM	David Wilcox		Talked
	8:12 AM	Bob Rubin		Talked
	7:57 AM	Kevin Warsh		Talked
	7:44 AM	Rodgin Cohen		Talked
9/23/2008	8:52 PM	Secretary Paulson		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
9/23/2008	8:02 PM	Larry Summers	[redacted]	Talked
9/23/2008	6:58 PM	Chairman Cox		Talked
9/23/2008	6:52 PM	Michelle Smith		Talked
9/23/2008	6:45 PM	Governor Warsh		Talked
9/23/2008	6:24 PM	Dan Jester		Talked
9/23/2008	6:26 PM	Tom Nides		Talked
9/23/2008	6:04 PM	Lloyd Blankfein		Talked
9/23/2008	5:58 PM	Secretary Paulson		Talked
9/23/2008	5:20 PM	Alan Greenspan		Talked
9/23/2008	5:15 PM	Secretary Paulson		Talked
9/23/2008	4:58 PM	Jeff Lacker		Talked
9/23/2008	4:46 PM	Bob Rubin		Talked
9/23/2008	4:42 PM	Bob Rubin		Talked
9/23/2008	3:47 PM	Stanley Fisher		Talked
9/23/2008	3:25 PM	Chairman Bernanke		Talked
9/23/2008	3:18 PM	Michelle Smith		Talked
9/23/2008	2:57 PM	David Wilcox		Talked
9/23/2008	2:47 PM	Eric Rosengren		Talked
9/23/2008	2:21 PM	Tim Long (OCC)		Talked
9/23/2008	2:17 PM	Larry Summers		Xfered to WLR
9/23/2008	2:04 PM	Jeff Immelt		Talked
9/23/2008	1:49 PM	Bev Hirtle		Talked
9/23/2008	1:34 PM	John Dugan		Talked
9/23/2008	1:21 PM	Tim Collins		Talked
9/23/2008	1:15 PM	Lloyd Blankfein		Talked
9/23/2008	12:51 PM	Steve Friedman		Talked
9/23/2008	12:32 PM	Katy Sparks		Talked
9/23/2008	11:51 AM	Vice Chair Kohn		Talked
9/23/2008	11/48 AM	Spence Hilton		Talked
9/23/2008	11:37 AM	Ed Forst		Talked
9/23/2008	11:27 AM	Rodgin Cohen		Talked
9/23/2008	11:18 AM	Larry Fink		Talked
9/23/2008	10:58 AM	Dick Fuld		Talked
9/23/2008	9:48 AM	Jean-Claude Trichet		Xfered to TJC
9/23/2008	9:32 AM	Alan Greenspan		Talked
9/23/2008	7:51 AM	Michelle Smith		Talked
9/23/2008	7:43 AM	Kevin Warsh		Talked
9/22/2008	7:03 PM	Steve Friedman		Talked
	7:01 PM	John Mack		Talked
	6:52 PM	Lloyd Blankfein		Talked
	6:50 PM	Jamie Dimon		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	6:42 PM	David Viniar	[redacted]	Talked
	6:31 PM	Michael "Mickey" Kantor (Former Secy of Commerce)	[redacted]	Talked
	6:22 PM	Mayor Bloomberg	[redacted]	Talked
	6:10 PM	Scott Alvarez	[redacted]	Talked
	6:01 PM	Bill Dudley	[redacted]	Talked
	5:53 PM	Scott Alvarez	[redacted]	Talked
	5:06 PM	Chairman Bernanke	[redacted]	Talked
	4:29 PM	Secretary Paulson	[redacted]	Talked
	4:25 PM	Bob Kelly	[redacted]	Talked
	3:03 PM	Don Donahue	[redacted]	Talked
	2:56 PM	Stephanie Heller	[redacted]	Talked
	2:53 PM	Secretary Paulson	[redacted]	Talked
	2:44 PM	Tom Nides	[redacted]	Talked
	2:34 PM	Checki	[redacted]	Talked
	12:57 PM	Bob Rubin	[redacted]	Talked
	12:08 PM	Alan Greenspan	[redacted]	Talked
	11:09 AM	Alan Greenspan	[redacted]	Talked
	10:54 AM	Don Kohn	[redacted]	Talked
	10:30 AM	Massimo Calabresi (Time Magazine)	[redacted]	Talked
	10:10 AM	Bob Rubin	[redacted]	Talked
	10:05 AM	Rahm Emanuel	[redacted]	Talked
	9:47 AM	Hector Sants	[redacted]	Talked
	9:39 AM	Secretary Paulson	[redacted]	Talked
	9:33 AM	Josef Ackerman	[redacted]	Talked
	9:30 AM	John Thain	[redacted]	Talked
	8:32 AM	Jamie Dimon	[redacted]	Talked
	8:25 AM	Vikram Pandit	[redacted]	Talked
	8:17 AM	Secretary Paulson	[redacted]	Talked
	8:17 AM	Rodgin Cohen	[redacted]	Talked
	8:09 AM	Jeff Immelt	[redacted]	Talked
	8:00AM	Chairman Bernanke	[redacted]	Talked
	7:56 AM	Lloyd Blankfein	[redacted]	Talked
	7:40 AM	John Mack	[redacted]	Talked
	7:27 AM	John Mack	[redacted]	Talked
9/21/2008	10:26 PM	John Mack	[redacted]	Talked
	8:58 PM	John Mack	[redacted]	Talked
	8:53 PM	John Mack	[redacted]	Talked
	8:49 PM	Chairman Cox	[redacted]	Talked
	8:40 PM	John Mack	[redacted]	Talked
	8:32 PM	Chairman Bernanke	[redacted]	Talked
	8:22 PM	Chairman Cox	[redacted]	Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	8:12 PM	Mayor Bloomberg	[redacted]	Talked
	8:07 PM	Don Kohn		Talked
	8:00 PM	Secretary Paulson		Talked
	7:56 PM	Secretary Paulson		Talked
	7:40 PM	John Mack		Talked
	7:33 PM	Rodgin Cohen		Talked
	7:11 PM	Jamie Dimon		Talked
	7:05 PM	Chairman Bernanke		Talked
	6:59 PM	Lloyd Blankfein		Talked
	6:31 PM	Rodgin Cohen		Talked
	6:25 PM	Chairman Bernanke		Talked
	6:23 PM	Tom Nides		Talked
		Senator Dodd		Talked
	6:00 PM	Rodgin Cohen		Talked
	5:58 PM	Charles Shumer		Talked
	5:56 PM	John Mack		Talked
	5:46 PM	Chairman Bernanke		Talked
	5:31 PM	John Winkelreid		Talked
	5:20 PM	Secretary Paulson		Talked
	5:09 PM	John Varley		Talked
	5:05 PM	Chairman Bernanke		
	5:04 PM	Secretary Paulson		Talked
	4:45 PM	Secretary Paulson & Chairman Bernanke		Talked
	4:40 PM	David Bonderman		Talked
	4:33 PM	Bob Rubin		Talked
	4:27 PM	Rodgin Cohen		Talked
	4:22 PM	Lloyd Blankfein		Talked
	3:50 PM	Secretary Paulson & Chairman Bernanke Initiated by Paulson)		Talked
	3:27 PM	Secretary Paulson & Chairman Bernanke & J. Mack		Talked
	3:13 PM	Secretary Paulson & Chairman Bernanke & J. Dimon		Talked
	3:06 PM	Secretary Paulson & Chairman Bernanke		Talked
	2:30 PM	Secretary Paulson		Talked
	2:21 PM	Secretary Paulson		Talked
	2:15 PM	Lloyd Blankfein		Talked
	2:05 PM	Jamie Dimon		Talked
	1:44 PM	Vikram Pandit		Talked
	1:34 PM	John Mack		Talked
	1:25 PM	Larry Summers		Talked
	1:20 PM	John Mack		Talked
	12:59 PM	Chairman Cox		Talked
	12:59 PM	Lloyd Blankfein		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	12:56 PM	Secretary Paulson	[redacted]	
	12:54 PM	Rodgin Cohen	[redacted]	Talked
	12:47 PM	Lloyd Blankfein	[redacted]	Talked
	12:20 PM	John Dugan	[redacted]	Talked
	12:11 PM	Secretary Paulson	[redacted]	Talked
	12:02 PM	Lloyd Blankfein	[redacted]	Talked
	11:47 AM	John Mack	[redacted]	Talked
	11:37 AM	Secretary Paulson	[redacted]	Talked
	11:16 AM	Chairman Bernanke	[redacted]	Talked
	11:11 AM	John Mack	[redacted]	Talked
	11:09 AM	Secretary Paulson	[redacted]	Talked
	11:01 AM	Michelle Smith	[redacted]	Talked
	10:27 AM	Larry Summers	[redacted]	Talked
	10:24 AM	Lloyd Blankfein	[redacted]	Talked
	10:15 AM	Lloyd Blankfein	[redacted]	Talked
	10:05 AM	Secretary Paulson	[redacted]	Talked
	10:02 AM	Chairman Bernanke	[redacted]	Talked
	9:52 AM	Chairman Bernanke	[redacted]	Talked
	9:45 AM	Jamie Dimon	[redacted]	Talked
	9:36 AM	Vikram Pandit	[redacted]	Talked
	9:24 AM	Kevin Warsh	[redacted]	Talked
	8:55 AM	Steve Shafran, Treasury	[redacted]	Talked
	8:49 AM	John Mack	[redacted]	Talked
	8:31 AM	Lloyd Blankfein	[redacted]	Talked
	8:22 AM	Dave McCormick	[redacted]	Talked
9/20/2008	9:28 PM	Secretary Paulson	[redacted]	Talked
	8:53 PM	Kevin Warsh	[redacted]	Talked
	8:45 PM	Secretary Paulson	[redacted]	Talked
	7:34 PM	Theo Lubke	[redacted]	Talked
	8:25 PM	Rodgin Cohen	[redacted]	Talked
	7:16 PM	Chairman Bernanke	[redacted]	Talked
	6:40 PM	Lloyd Blankfein	[redacted]	Talked
	6:26 PM	Vikram Pandit	[redacted]	Talked
	6:13 PM	Vikram Pandit	[redacted]	Talked
	6:11 PM	Secretary Paulson	[redacted]	Talked
	6:07 PM	Jamie Dimon	[redacted]	Talked
	5:26 PM	Secretary Paulson	[redacted]	Talked
	5:07 PM	Lloyd Blankfein	[redacted]	Talked
	5:02 PM	Jamie Dimon	[redacted]	Talked
	4:17 PM	John Mack	[redacted]	Talked
	4:08 PM	Lloyd Blankfein	[redacted]	Talked
			[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	3:50 PM	Lloyd Blankfein	[redacted]	Talked
	3:17 PM	Secretary Paulson		Talked
	3:02 PM	Bob Rubin		Talked
	2:50 PM	Secretary Paulson		Talked
	2:53 PM	Lloyd Blankfein		Talked
	2:36 PM	Vikram Pandit		Talked
	2:30 PM	Dick Parson		Talked
	2:17 PM	Lloyd Blankfein		Talked
	2:04 PM	Hector Sants (Cumming/Baxter talked to Mr. Sants)		Talked
	1:58 PM	Secretary Paulson		Talked
	1:31 PM	Secretary Paulson		Talked
	1:20 PM	Jamie Dimon		Talked
	1:21 PM	Ken Wilson		Talked
	1:14 PM	Rodgin Cohen		Talked
	1:10 PM	Lloyd Blanklein		Talked
	1:08 PM	John Mack		Talked
	12:52 PM	Congressman Rahm Emaunel		Talked
	12:45 PM	Secretary Paulson		Talked
	12:41 PM	John Mack		Talked
	12:36 PM	Lloyd Blankfein		Talked
	11:24 AM	Mario Draghi		Talked
	11:13 AM	Chairman Cox		Talked
	10:21 AM	Chairman Bernanke		Talked
	10:19 AM	Congressman Rahm Emaunel		Talked
	9:58 AM	Josh Steiner		Talked
	9:34 AM	Colm Kelleher (CFO Morgan Stanley), et al		Talked
	9:30 AM	Secretary Paulson		Talked
	9:24 AM	Secretary Paulson		Talked
	9:20 AM	Don Kohn		Talked
	9:02 AM	Lloyd Blanklein		Talked
	8:56 AM	John Mack		Talked
	8:43 AM	Rodgin Cohen		Talked
	8:10 AM	Dan Jester & Ken Wilson		Talked
	7:00 AM	Hector Sants (C. Cumming - talked)		Talked
9/19/2008	9:37 PM	Dan Jester		Talked
	8:48 PM	Tom Baxter		Talked
	8:31 PM	Dan Jester		Talked
	8:17 PM	Secretary Paulson		Talked
	8:04 PM	Chairman Cox		Talked
	7:57 PM	Senator Dodd		Talked
	7:35 PM	Lloyd Blankfein		Talked

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TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	7:15 PM	Meg Mcconnell	[redacted]	Talked
	7:10 PM	Anka / Volcker		Talked
	6:54 PM	Rodgin Cohen		Talked
	6:50 PM	Lloyd Blankfein		Talked
	6:40 PM	Bernanke & Paulson		Talked
	6:32 PM	Don Kohn		Talked
	5.58 PM	Chairman Bernanke		Talked
	5:46 PM	Don Kohn		Talked
	5:39 PM	Bob Kelly		Talked
	5:29 PM	Secretary Paulson		Talked
	5:23 PM	Michelle Smith		Talked
	4:51 PM	Calvin Mitchell		Talked
	4:36 PM	Charles Wait		Talked
	4:32 PM	Seth Waugh		Talked
	4:16 PM	John Mack		Talked
	3.50 AM	Steven Shafran		Talked
	3:27 PM	John Dugan		Talked
	3:08 PM	Charles Wait		Talked
	2.13 PM	Kevin Warsh		Talked
	1.39 PM	Louise Roseman		Talked
	1:06 PM	David Viniar		Talked
	12:40 PM	Josh Bolten (Chief of Staff to President)		Talked
	12:12 PM	Hector Sants (Baxter took call when TFG could not)		Talked
	11:47 AM	Charles Wait		Talked
	11:31 AM	Lloyd Blankfein		Talked
	11:29 AM	Steven Shafran		Talked
	10:33 AM	Don Kohn		Talked
	10:12 AM	John Mack		Talked
	9:57 AM	Jon Cunliffe		Talked
	9:54 AM	Paulson		Talked
	9:50 AM	Jon Cunliffe		Talked
	9:35 AM	Jamie Dimon		Talked
	9:30 AM	Jeff Immelt		Talked
	9:20 AM	Steve Friedman		Talked
	9:14 AM	Vikram Pandit		Talked
	9:04 AM	Mr. Henri Decastries, Chair & CEO Axa Group		Talked
	9:00 AM	Hector Sants		Talked
	9:00 AM	Chris Burke		Talked
	8:51 AM	Hector Sants		Talked
	8:45 AM	Scott Alvarez		Talked
	8:35 AM	Paulson		Talked

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REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	8:26 PM	Checki	[redacted]	Talked
	8:26 AM	Chairman Cox	[redacted]	Talked
	8:14 AM	Lloyd Blankfein	[redacted]	Talked
	8:10 AM	Jean-Claude Trichet	[redacted]	Talked
	8:06 AM	Dick Fuld	[redacted]	Talked
	8:06 AM	Peter Fisher spoke to Dudley	[redacted]	Talked
	7:51 AM	John Dugan	[redacted]	Talked
	7:48 AM	Bob Diamond	[redacted]	Talked
	7:48 AM	Lee Sachs	[redacted]	Talked
	7:38 AM	Lee Sachs	[redacted]	Talked
	per TFG	Michele Smith	[redacted]	Talked
	per TFG	Ralph Schlosstein	[redacted]	Talked
	per TFG	John Thain	[redacted]	Talked
9/18/2008	10:28 PM	David Nason	[redacted]	Talked
	9:58 PM	John Mack	[redacted]	Talked
	9:54 PM	Eric Sirri	[redacted]	Talked
	9:08 PM	Lloyd Blankfein	[redacted]	Talked
	9:04 PM	Secretary Paulson	[redacted]	Talked
	7:56 PM	John Mack	[redacted]	Talked
	7:10 PM	John Dugan	[redacted]	Talked
	6:56 PM	Don Kohn	[redacted]	Talked
	6:47 PM	John Mack	[redacted]	Talked
	6:13 PM	Steve Shafran	[redacted]	Talked
	6:13 PM	Secretary Paulson	[redacted]	Talked
	6:11 PM	Chairman Bernanke	[redacted]	Talked
	6:09 PM	Jim Wilkinson	[redacted]	Talked
	6:01 PM	Brian Leach	[redacted]	Talked
	5:51 PM	Jamie Dimon	[redacted]	Talked
	5:42 PM	Secretary Paulson	[redacted]	Talked
	5:23 PM	John Mack	[redacted]	Talked
	5:18 PM	Jon Cunliffe	[redacted]	Talked
	5:12 PM	Lloyd Blankfein	[redacted]	Talked
	5:04 PM	Jamie Dimon	[redacted]	Talked
	4:34 PM	Chairman Bernanke	[redacted]	Talked
	4:30 PM	Jamie Dimon	[redacted]	Talked
	4:25 PM	John Mack	[redacted]	Talked
	4:15 PM	Secretary Paulson	[redacted]	Talked
	2:47 PM	Bob Kelly	[redacted]	Talked
	1:11 PM	Nancy Stroker, Fitch	[redacted]	Talked
	1:08 PM	Secretary Paulson	[redacted]	Talked
	1:06 PM	Ken DeRegt	[redacted]	Talked

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TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	12:56 PM	Rita Bolger and Vicky Tillman, S&P	[redacted]	Talked
	12:53 PM	Vikram Pandit		Talked
	12:32 PM	John Mack		Talked
	12:27 PM	Secretary Paulson		Talked
	12:04 PM	Secretary Paulson		Talked
	11:49 AM	Secretary Paulson		Talked
	11:33 AM	Don Kohn		Talked
	11:06 AM	Gov Warsh		Talked
	10:52 AM	Chairman Bernanke		Talked
	10:17 AM	Chairman Cox		Talked
	9:16 AM	Bernanke, Kohn, Warsh		Talked
	9:06 AM	Chairman Bernanke		Talked
	9:00 AM	Secretary Paulson		Talked
	8:55 AM	Lloyd Blankfein		Talked
	8:57 AM	Gov Warsh		Talked
	8:41 AM	Chairman Bernanke		Talked
	8:38 AM	Secretary Paulson		Talked
	8:30 AM	Secretary Paulson		Talked
	8:23 AM	Lloyd Blankfein		Talked
	8:20 AM	Lloyd Blankfein		Talked
	8:15 AM	Jamie Dimon		Talked
9/17/2008	10:54 PM	Larry Summers		Talked
	10:50 PM	Scott Alvarez		Talked
	10:39 PM	Jim Wilkinson		Talked
	10:11 PM	Don Kohn		Talked
	9:59 PM	Calvin Mitchell		Talked
	9:57 PM	Don Kohn		Talked
	9:34 PM	Jeff Immelt		Talked
	8:19 PM	Don Kohn		Talked
	8:13 PM	Cathy Cassidy (GE) - Meg Talked		Talked
	7:30 PM	Call w/Paulson		Talked
	7:07 PM	Lloyd Blankfein		Talked
	6:59 PM	Lloyd Blankfein		Talked
	6:47 PM	Rodgin cohen		Talked
	6:42 PM	Bob Steel		Talked
	6:31 PM	Jamie Dimon		Talked
	6:27 PM	Bob Greenhill		Talked
	6:25 PM	Secretary Paulson		Talked
	5:45 PM	Chairman Bernanke & Don Kohn		Talked
	5:30 PM	Don Kohn		Talked
	5:14 PM	Chairman Cox		Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	5:09 PM	Chairman Cox	[redacted]	Talked
	5:03 PM	Edward Liddy (Willumstad's replacement)		Talked
	5:01 PM	Don Kohn		Talked
	4:47 PM	Paulson		Talked
	4:27 PM	Mike Neal & Cathy Cassidy, GE		Talked
	4:23 PM	Bob Rubin		Talked
	4:00 PM	Jeff Immelt		Talked
	4:15 PM	Bob Kelly		Talked
	4:11 PM	William Dudley		Talked
	2:29 PM	Jamie Dimon		Talked
	2:20 PM	Don Kohn		Talked
	2:10 PM	Bob Kelly		Talked
	1:46 PM	Don Kohn		Talked
	1:19 PM	Blankfein		Talked
	12:49 PM	Paulson		Talked
	12:15 PM	Paulson		Talked
	12:10 PM	Chairman Bernanke		Talked
	10:41 AM	Peter Fisher		Talked
	10:39 AM	Secretary Paulson		Talked
	10:35 AM	Ken DeRegt		Talked
	10:33 AM	Secretary Paulson		Talked
	10:29 AM	Chairman Cox		Talked
	9:41 AM	Secretary Paulson		Talked
	9:40 AM	Gov Warsh		Talked
	9:32 AM	Michelle Smith		Talked
	8:18 AM	Dan Jester		Talked
	8:17 AM	Dan Jester		Talked
	8:17 AM	John Mack		Talked
	8:10 AM	Sheila Bair		Talked
	8:16 AM	Jamie Dimon		Talked
	8:15 AM	Jamie Dimon		Talked
	7:59 AM	Larry Fink		Talked
	7:56 AM	John Thain		Talked
	7:49 AM	Brian Leach		Talked
	7:48 AM	Secretary Paulson		Talked
	7:44 AM	Lloyd Blankfein		Talked
	7:39 AM	Jamie Dimon		Talked
	7:31 AM	Chairman Cox		Talked
	7:22 AM	Secretary Paulson		Talked
9/16/2008	10:00 PM	Charles O'Byrne (Gov. Patterson's office)		Talked
	9:36 PM	Bob Willumstad		Talked

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TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	9:05 PM	Charles O'Byrne (Gov. Patterson's office)	[redacted]	Talked
	8:57 PM	Mayor Bloomberg	[redacted]	Talked
	8:39 PM	Ken Wilson	[redacted]	Talked
	8:32 PM	Don Kohn	[redacted]	Talked
	8:20 PM	Secretary Paulson & Chairman Bernanke	[redacted]	Talked
	7:54 PM	Bob Willumstad	[redacted]	Talked
	7:42 PM	Sec'y Paulson	[redacted]	Talked
	7:12 PM	John Reich	[redacted]	Talked
	7:03 PM	Don Kohn	[redacted]	Talked
	6:55 PM	Eric Dinallo	[redacted]	Talked
	6:46 PM	Dan Jester	[redacted]	Talked
	6:25 PM	Jamie Dimon	[redacted]	Talked
	6:16 PM	Chairman Bernanke	[redacted]	Talked
	6:00 PM	Michele Smith	[redacted]	Talked
	5:14 PM	Steve Friedman	[redacted]	Talked
	5:01 PM	William Dudley	[redacted]	Talked
	4:29 PM	Chairman Bernanke	[redacted]	Talked
	4:27 PM	Gov Warsh	[redacted]	Talked
	4:20 PM	Hank Paulson	[redacted]	Talked
	3:49 PM	Vikram Pandit	[redacted]	Talked
	3:38 PM	Eric Dinallo	[redacted]	Talked
	3:30 PM	Rham Emanuel	[redacted]	Talked
	3:17 PM	Don Kohn	[redacted]	Talked
	2:30 PM	Call w/Bernanke and Paulson, et al	[redacted]	Talked
	2:26 PM	Chairman Bernanke	[redacted]	Talked
	2:24 PM	Chris Burke et al	[redacted]	Talked
	2:04 PM	Secretary Paulson	[redacted]	Talked
	1:47 PM	Bob Diamond (cell)	[redacted]	Talked
	1:43 AM	Dan Jester	[redacted]	Talked
	1:41 PM	Jean-Claude Trichet	[redacted]	Talked
	1:38 PM	Eric Dinallo	[redacted]	Talked
	1:22 PM	Bill Dudley	[redacted]	Talked
	1:19 PM	Chairman Bernanke	[redacted]	Talked
	1:17 PM	Eric Dinallo	[redacted]	Talked
	1:14 PM	Jamie Dimon	[redacted]	Talked
	1:08 PM	Dan Jester (cell)	[redacted]	Talked
	1:00 PM	John Rich, Dir., Office of Thrift Supervision	[redacted]	Talked
	12:33 PM	Chairman Bernanke	[redacted]	Talked
	12:10 PM	Callum McCarthy	[redacted]	Talked
	11:39 AM	Robert Willumstad	[redacted]	Talked
	11:36 AM	Senator Charles Schumer	[redacted]	Talked

REDACTED

TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	11:32 AM	Secretary Paulson	[redacted]	
	11:30 AM	Scott Alvarez	[redacted]	Talked
	11:24 AM	Calvin Mitchell	[redacted]	Talked
	11:17 AM	Willumstad & Rodgin Cohen	[redacted]	Talked
	11:17 AM	Secretary Paulson	[redacted]	Talked
	10:58 AM	Chairman Bernanke	[redacted]	Talked
	10:53 AM	Scott Alvarez	[redacted]	Talked
	10:49 AM	Vikram Pandit	[redacted]	Talked
	10:29 AM	Secretary Paulson	[redacted]	Talked
	10:27 AM	Chairman Cox	[redacted]	Talked
	10:16 AM	Warren Buffett	[redacted]	Talked
	10:01 AM	Lloyd Blankfein	[redacted]	Talked
	9:54 AM	Jean-Claude Trichet	[redacted]	Talked
	9:50 AM	Andrew Cuomo	[redacted]	Talked
	9:45 AM	Secretary Paulson	[redacted]	Talked
	9:39 AM	Rita Proctor	[redacted]	Talked
	9:31 AM	Chairman Chris Cox	[redacted]	Talked
	9:27 AM	J. Dimon	[redacted]	Talked
	9:20 AM	Vikram Pandit	[redacted]	Talked
	9:16 AM	Lloyd Blankfein	[redacted]	Talked
	9:14 AM	Mayor Michael Bloomberg	[redacted]	Talked
	9:13 AM	Bob Kelly	[redacted]	Talked
	8:40 AM	Lloyd Blankfein	[redacted]	Talked
	8:00 AM	Chairman Bernanke and Secy. Paulson	[redacted]	Talked
	7:50 AM	Chairman Bernanke	[redacted]	Talked
	7:45 AM	Bob Kelly, BONY	[redacted]	Talked
9/15/2008	10:10 PM	Erik Sirri	[redacted]	Talked
	9:05 PM	Tony Ryan & V C. Kohn	[redacted]	Talked
	8:18 PM	Michelle Smith	[redacted]	Talked
	7:15 PM	Governor Shirakawa, Bank of Japan	[redacted]	Talked
	7:56 PM	Secretary Paulson	[redacted]	Talked
	6:34 PM	Hillary Clinton	[redacted]	Talked
	6:20 PM	Secretary Paulson	[redacted]	Talked
	6:20 PM	Don Kohn	[redacted]	Talked
	6:16 PM	Secretary Paulson	[redacted]	Talked
	6:07 PM	Bob Kelly	[redacted]	Talked
	5:52 PM	Dan Jester	[redacted]	Talked
	5:38 PM	Peter Fischer, Blackrock	[redacted]	Talked
	5:32 PM	Lloyd Blankfein	[redacted]	Talked
	5:26 PM	Hamid Biglari, Citigroup	[redacted]	Talked
	5:05 PM	Josh Steiner	[redacted]	Talked
			[redacted]	Talked

REDACTED

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TALK SHEET

Talked DATE	TIME	CALLER	PHONE #	MESSAGE
	5:04 PM	Dan Jester	[redacted]	Talked
	4:58 PM	Gov David Patterson	[redacted]	Talked
	4:04 PM	Chairman Bernanke	[redacted]	Talked
	3:58 PM	Brady Dougan, Credit Suisse	[redacted]	Talked
	4:23 PM	Peter Kraus	[redacted]	Talked
	3:57 PM	Dan Jester	[redacted]	Talked
	3.52 PM	Bob Diamond	[redacted]	Talked
	3:49 PM	John Thain	[redacted]	Talked
	3:40 PM	Jeff Immelt	[redacted]	Talked
	3:36 PM	Hank Greenberg	[redacted]	Talked
	3:31 PM	Meg Mcconnell	[redacted]	Talked
	3:27 PM	Meg Mcconnell	[redacted]	Talked
	3:23 PM	Larry Fink	[redacted]	Talked
	3.05 PM	Lee Sachs	[redacted]	Talked
	2:52 PM	Chairman Bernanke	[redacted]	Talked
	2:37 PM	Secretary Paulson	[redacted]	Talked
	2:34 PM	Vikram Pandit	[redacted]	Talked
	1:45 PM	Callum McCarthy	[redacted]	Talked
	1:42 PM	Barry Zubrow (J. Dimon's office)	[redacted]	Talked
	1:34 PM	Congressman Barney Frank	[redacted]	Talked
	1:28 PM	Jamie Dimon	[redacted]	Talked
	12:43 PM	Jeff Lacker	[redacted]	Talked
	12.38 PM	Hildebrand	[redacted]	Talked
	12:30 PM	Paul Volcker	[redacted]	Talked
	11:50 PM	Chairman Cox	[redacted]	Talked
	11:27 AM	Pete Pettersen	[redacted]	Talked
	11:21 AM	Charles O'Byrne (Gov. Patterson's office)	[redacted]	Talked
	10:59 AM	Jerry Corrigan	[redacted]	Talked
	10:58 AM	Hank Paulson	[redacted]	Talked
	10:50 AM	Michael Bloomberg	[redacted]	Talked
	10:36 AM	Eric Dinallo	[redacted]	Talked
	10:33 AM	Hank Paulson	[redacted]	Talked
	10:25 AM	Chuck Schumer	[redacted]	Talked
	10:19 AM	Bob Willumstad	[redacted]	Talked
	9:56 AM	Jerry Corrigan	[redacted]	Talked
	8:51 AM	Masaaki Shirakwa, Bank of Japan	[redacted]	Talked
	8:05 AM	Hank Paulson	[redacted]	Talked
	8:01 AM	Mervyn King, BOE	[redacted]	Talked
	7:38 AM	Jean-Claude Trichet	[redacted]	Talked
	7:30 AM	Dan Jester/Hank Paulson (spoke with Paulson)	[redacted]	Talked
9/14/2008	10:39 AM	Hank Paulson	[redacted]	Talked

Ms. KAPTUR [continuing]. November 26th—thank you, Mr. Chairman—the critical period when the bailout occurred, and just after September 15th, when the three major rating agencies downgraded AIG's credit rating, you made hundreds of calls, and the most, over 225, to Secretary Paulson, who was then Secretary of the Treasury. What firm did he work for prior to his appointment as Secretary of Treasury?

Secretary GEITHNER. He worked for Goldman Sachs.

Ms. KAPTUR. He worked for Goldman Sachs. Now, Goldman Sachs, as I understand it, got the most in counterparty payments of any domestic institution, is that true, $14 billion?

Secretary GEITHNER. I actually don't know if that is true, but that is a matter of public record.

Ms. KAPTUR. Societe Generale got the most from an international firm, but Goldman Sachs was No. 1. Now, you made about 100 calls to Fed Chair Ben Bernanke, but then the next highest number of calls in that period, you made 103——

Chairman TOWNS. The gentlewoman's time has expired.

Ms. KAPTUR —to a man named Dan Jester.

Chairman TOWNS. Will the lady summarize?

Ms. KAPTUR. Mr. Chairman, may I just ask what firm did he work for?

Secretary GEITHNER. As you know, he worked for Goldman Sachs.

Ms. KAPTUR. Thank you. And I will have additional questions with regard to who you phoned and we will place that in the record. Thank you.

[The information referred to follows:]

Memo to File

Date:	October 2, 2008
To:	Tom Baxter, Executive Vice President and General Counsel
From:	Sarah Dahlgren, Senior Vice President
Sub:	Request to engage BlackRock Solutions

In connection with the formation of Maiden Lane II and Maiden Lane III, (collectively, the "Entities"), the Federal Reserve Bank of New York (the "FRB-NY") requests the authorization to engage BlackRock Solutions ("BlackRock") to perform the following contemplated services:

1. Perform a fair value assessment and risk analysis on the AIG FP portfolio of CDS on CDO's transactions to be placed in Maiden Lane III.
2. Perform a fair value assessment and risk analysis on the portfolio of investments purchased in connection with the Securities Lending Program to be placed in Maiden Lane III.
3. Assist with the formation and structuring of the Entities.
4. Potentially become the asset manager of the Entities.

BlackRock is intimate with the details of the CDS on CDO's within AIG FP as a result of it being recently engaged by AIG to provide cash flow projections on a significant portion of the portfolio.

Additionally, BlackRock's Financial Markets Advisory Group is a world class leader in this field and has managed or advised on distressed structured finance portfolios totaling over $250 billion since mid-2007. BlackRock also worked with the FRB-NY on the $30 billion facility related to the JP Morgan/Bear Stearns merger, and currently works with many investment banks, insurers and global commercial banks.

BlackRock has been in discussions with AIG, Inc. to be engaged to perform services similar to those described above in items #1 and #2 above on AIG's behalf. To the best of our knowledge, BlackRock has not been engaged by AIG Inc. as of the preparation of this memorandum.

As a result of the word class organization, industry experience and familiarity with the portfolios contemplated for inclusion within the Entities, along with the need for the timely and efficient engagement of a service provider, our recommendation would be to engage BlackRock to perform the contemplated services.

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.
SECRETARY OF THE TREASURY

October 8, 2008

Timothy F. Geithner
President
Federal Reserve Bank of New York
33 Liberty Street
New York, New York 10045

Tim
Dear Mr. Geithner:

During this period of financial turmoil, we have worked together to enhance the stability, liquidity and orderliness of our financial markets. Over the past several months, it became clear that the situation at AIG presented a substantial and systemic threat to those financial markets.

I believe the Federal Reserve Bank of New York's provision of a special liquidity facility to AIG in order to allow the company to meet its obligations was necessary to prevent the substantial disruption to financial markets and the economy that could well have occurred from a disorderly wind-down of AIG. On behalf of the Department of the Treasury, I fully support the FRBNY's action and acknowledge that, if any loss arises out of this facility, the loss will be treated by the FRBNY as an expense that may reduce the net earnings transferred by the FRBNY to the Treasury general fund.

I look forward to working with the Federal Reserve to put in place a comprehensive framework for addressing systemic risk in the financial system. An important part of this will entail a framework for dealing with the threats to the stability of the financial system posed by the precipitous failure of large complex financial institutions.

Sincerely,

Henry M. Paulson, Jr.

Meg McConnell/NY/FRS
10/22/2008 11:05 PM

To Timothy Geithner/NY/FRS@FRS
cc Michael Silva/NY/FRS@FRS
bcc
Subject Call tonight with Board staff

I sat in on the AIG call with Board staff at 7:30 (originally scheduled for 7 but moved to 7:30 so that Jester could spend a half an hour telling Sarah that there will be no capital and that we need to make "something else" work).
Before and after that call, the team explained to me a bit more about ML 2 and 3, and 3 in particular. Some things that I noted:

1. The new ML 3--in which they tear up the CDS and purchase the underlying CDOs--seems pretty good from a financial stability perspective (if it can be done), better then the original one they'd proposed bc it seems to remove considerably more uncertainty for the firms and arguably for the system. Some outstanding issues around this are:
- The discrepancy bw what our advisors are saying these CDO's are worth and where the firms have them marked.
- The degree to which we'd want to push the firms that would sell CDOs to the structure to put up a mezz tranche that would either (or both?) cushion our exposure or reduce the size of the equity required from AIG in the structure.
- To what extent do AIG's CDS counterparties actually hold the underlying CDO's on their books? My impression is that for a bunch of the European banks the answer might be yes, but for others it's not clear, and may lean a little more toward no. I think this could matter for actually being able to get this done, but I'm not sure.

2. Leaving aside Treasury's unfortunate (untenable?) stance on this, Board staff still doesn't seem to be attacking this in a "here's what we need to do and why" kind of way. I know they've been much more supportive very recently, but given what's at stake and the speed with which a bunch of decisions need to be made to avoid a bad rating outcome, they seem not quite as focused on helping us sort out the thorny bits as they could be. Some of the things that I noted on this from the call:

- On ML2 and ML3, the staff noted that the lawyers were still not quite "there" on 2, let alone on 3. Not clear what they are waiting for on these things, but it seems like they should say yes or no fast because we're running out of time to devise new structures
- Getting the right balance of extending the term and lowering the rate on the facility. Here there was a view that lowering the rate would be too "provocative", so extending term would be better. The point was made that we need both, but I wasn't clear whether they fully appreciated this.
- Neither Treasury nor us can provide guarantees. Treasury bc of scoring and us for the usual reasons. So the presumption was that keepwells are off the table.
- Neither Treasury nor us can put capital in. I guess Tom is calling Scott to talk through the subordination issue, though Sarah stressed that leverage ratio constraints meant that some form of equity and not debt was required.

Overall, what seemed to be missing in the way Board staff talked with our team about these issues was an appreciation of the fact that without making some combination of all or at least most of these things happen within a very short period of time, the firm will be downgraded and we'll be forced to do way more on all those fronts. And that maybe even if we did way more on all these fronts, a downgrade would lead to a default and we'd undo all that's been done from a financial stability perspective over the last two weeks, and we'd lose the public's trust at a really bad time to lose it. I hope they see the potential for that scenario to be just as "provocative" to Congress as one in which we take the rate down from this crazily high one that was forced on us (meaning FRBNY) by people that have since punted on all the hard things that came about as a result of the decision to lend that all of us knowingly made together that weekend.

Again, my sense is that Board staff is listening to our guys and is generally supportive of their effort, but they seem to be operating under the assumption that we have way more wiggle room on this than I understand us to have. Anyway, I think you know all this, but I wanted to pass along my impressions in advance of the calls tomorrow.

Margaret M. McConnell
Federal Reserve Bank of New York
212-720-6773

Sarah Dahlgren/NY/FRS
10/02/2008 12:08 PM

To: dan.jester@do.treas.gov, Timothy Geithner/NY/FRS@FRS, Michael Silva/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS
cc:
bcc:
Subject: follow up call from S&P

Spoke to Grace Osborne and Jay True (he runs the global finanancials institutions ratings for the company)....they had two clarifying questions:

1. Over the course of the next two weeks, was I/my team speaking with the "authorization" of the appropriate persons in Treasury and FRBNY to describe what we are planning and will be putting in place with AIG?

I explained that we had a rigorous process that involved many levels of vetting and sign-off across the agencies and that we would be moving forward on solutions only with the intent to execute the solutions that were legal and feasible (within whatever limitations we have). They seemed satisfied to know that we weren't going to be presenting them with solutions that weren't actually going to get signed off on by the appropriate authorities.

2. They wanted clarification about the subordination of the AIG senior debt holders. Their view is that the AIG FP obligors are senior to AIG's senior debt holders; their concern -- and what they have to explain to the market -- is that the senior debt holders of AIG are DEEPLY SENIOR to AIG FP and to the Fed.....here's the response that I sent back to S&P (provided by our legal counsel) to clarify for S&P:

"In terms of their claims on AIG Inc., the FP counterparties are pari passu with AIG Inc. senior unsecured debt. Both are junior to the Fed claim to the extent of the AIG Inc. collateral pledged to the Fed (principally stock of first-tier subsidiaries).

The FP counterparties of course have a claim at the FP level that neither AIG senior debt nor the Fed has, and have whatever collateral FP has posted.

The Fed of course has collateral and guarantees at various AIG subsidiaries that neither the AIG senior debt nor the FP counterparties have."

The discussion ended on a "positive" note...but no promises

* * * * * * * * * * * * * *

Sarah Dahlgren
Senior Vice President
Federal Reserve Bank of New York
212-720-7537 (work)
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914-738-9410 (home)

visit www.newyorkfed.org
* * * * * * * * * * * * * * *

Timothy Geithner/NY/FRS
10/15/2008 08:43 AM

To donald.kohn
cc
bcc Michael Silva/NY/FRS@FRS, [illegible] [illegible]/NY/FRS@FRS, Meg McConnell/NY/FRS@FRS, Kristin Mayer/NY/FRS@FRS
Subject Fw: AIG call tonight

Please don't circulate this

I thought you should see it though

This is an area where it would be useful to have some alternative ideas from Board staff and Governors rather than Board staff simply relaying the concerns of the Governors

----- Forwarded by Timothy Geithner/NY/FRS on 10/15/2008 08:43 AM -----

Sarah Dahlgren/NY/FRS
10/15/2008 12:50 AM

To Timothy Geithner/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS
cc Michael Silva/NY/FRS@FRS, Meg McConnell/NY/FRS@FRS, [illegible]/NY/FRS@FRS, Kristin Mayer/NY/FRS@FRS, Terrence Checki/NY/FRS@FRS, Christine Cumming/NY/FRS@FRS
Subject Fw: AIG call tonight

To bring you up to speed following our discussions earlier this evening ... we spent another hour with Board staff this evening on the way forward

1. We described the need for a broad set of solutions for the problem -- starting with the securities borrowing transaction last week, and indicated that it wasn't just one "fix" that was needed, but a package of things that

and raised the key issues at the firm (liquidity and capital)

2. We indicated that the programs announced this morning need to be assessed for applicability to AIG. Deborah Bailey confirmed that the FDIC wasn't looking to have AIG in the guarantee program longer than 30 days ... she also indicated that it wasn't clear that it was the FDIC's call; we indicated that we were in discussions with the firm on their analysis and that we were doing the same – but that additional clarity around all of them was needed, particularly since the agency press releases and other documents aren't all consistent across one another ... (we told them it didn't fix the problems, but possibly bought us some small amount of time)

3. We indicated that even with the programs announced this morning, we nevertheless needed to press forward on the set of solutions that we had in train – namely, ML 2 and ML 3, deal restructuring and options on capital, and keepwell/guarantee options – since it wasn't at all clear that any "bang" out of this morning's announcements would buy us anything other than a little time. *Board staff again reiterated that they didn't think that the Governors (unnamed) would go for ML 2 or ML 3; their ears perked up, though, when we indicated that ML 2 would be done only as an "out" for the securities borrowing transaction and wouldn't be an "add" to the current total of programs (so, 24 in RMBS in exchange for 37.8 instead); they continue to push back hard on ML 3*

4. We described the rating agency process that we were intending to follow – together with the firm – starting tomorrow with Step 1 and leading up to announcement of 3Q earnings on November 5 (this can be accelerated if need be depending on rating agency reactions, and any indications they are prepared to act)

Step 1: This week 10/13: two pieces to talk with the rating agencies about: a) discuss the Treasury/Fed/FDIC announcements in the context of AIG: new news, could have a positive impact, still needs to be assessed, work is being done to assess impact as well as garner more details on the options, etc. ... and b) discuss the RMBS structure option, essentially on a no-name basis (so, the FRBNY's name isn't on any of the slides the firm will be using) to elicit feedback from the rating agencies on the "total sec lending solution"

Step 2: Beginning of next week 10/20: two pieces here as well: a) open discussions on FP possibilities – essentially working through the ML 3 concepts and any other solutions that come through those discussions, and b) discussion on restructuring of loan terms (rate, ticking fee, maturity, etc. ...)

Step 3: End of next week 10/25: one piece: a) discussion of the capital options

Step 4: Beginning of 10/27: one piece: **a) keepwell/guarantee** ... *Board staff emphatically said this was off the table; we countered with questions about why it was so clearly off the table and suggested, as well, that perhaps this was something that Treasury could do ... they weren't willing to consider it – and suggested that we needed to do some work with Treasury to get them to do the keepwell/guarantee ... we think this is something we need to* *<u>have in our back pockets just for contingency purposes – if a ratings downgrade happens at any time in the next three weeks or afterwards, we will need this to protect any value in the insurance companies and, importantly, to avoid a disorderly seizure by regulators of the insurance companies (we'll provide more details on this in our bankruptcy discussion) ...</u>*

Board staff agreed with our plan to move ahead with Step 1; they are reluctant to give any go ahead on Step 2 (particularly ML 3/Financial Products solutions) and seemed open to talking about deal structure and capital options. *...the rating agencies, though, are going to be looking for the FP solutions sooner rather than later (the second fix for the latter liquidity bleed in the company)*

we agreed to talk again later in the week (meanwhile, we are continuing to include them in all discussions on ML 2 and ML 3, as well as other briefing opportunities)

Rich and Kieran ended on a relatively positive note (I'm looking for any positives these days) by indicating that they are willing to do what they can at Board staff; that there is a realization by the Governors that they may need to lend more to obviate the systemic risks and they aren't against lending more into a troubled situation if necessary to prevent systemic implications. Finally, either Kieran or Rich indicated that the Governors have cited the Bear Stearns deal as a one-off deal that was done on the understanding it wouldn't be done again (so ML 2 and ML 3 aren't well-received ...). We asked again – if they have other options that we should be putting on our list of things to consider, we're very open to that

We'll be coming back to you with our thinking on the restructuring of the deal and capital issues later in the week; we're making progress on that front even though we just started tonight, but should have something to share later in the week

<u>Questions that were asked repeatedly by staff on the call (but were attributed to Governors):</u>

1. What does any of this buy us?

2. **What if the rating agencies still downgrade the firm?** *(this is why they have to think much longer/harder on the keepwell/guarantee question)*

3. What are the systemic implications of a downgrade? *(clearly, this is still a "to do" for us as the Governors haven't gotten any more comfortable with answers thus far provided by Board staff; we are working on a presentation that we can walk through with them ... [illegible] ... at the beginning of next week ... [illegible] ... and provide input on the systemic implications of FP)*

4. **Treasury has communicated that it is not interested in doing anything for AIG. What is your next step here?** *(that was directed at the FRBNY)*

5. Aren't you using the leverage and influence that you have on the firm to be forcing them to use the money we are providing to them to FIX the problems? *(... [illegible] ...)*

Holler if you have questions or want to follow up more on any of these issues

Chairman TOWNS. Thank you very much.

Secretary GEITHNER. Mr. Chairman, could I just say one thing in response to this? I just want to say—it is very important.

Congresswoman, you were suggesting that the people who were involved in this were not acting in the public interest, and you were suggesting that they were working for the private interest, not the public interest, and that is not true. I would never, and I believe none of those individuals would ever be part of any decision like that. And I think these people were people of enormous integrity and experience operating under exceptional circumstances, with no precedent, doing the best they could for what was in the public interest.

Ms. KAPTUR. Well——

Secretary GEITHNER. And it is important to say for the record——

Chairman TOWNS. I must move. I must move. I must move.

The gentleman from Georgia, Congressman Westmoreland.

Mr. WESTMORELAND. Thank you, Mr. Chairman.

Secretary Geithner, when did AIG—if you could just give us a date—when did AIG call and say we need some money?

Secretary GEITHNER. Well, they came to Treasury and the Fed formally, I think, on that Friday, which was——

Mr. WESTMORELAND. Friday the——

Secretary GEITHNER. I think it was the—well, the calendar will show. It was the Friday in September, the 11th or the 12th, I think.

Mr. WESTMORELAND. OK. So it was a Friday in September? And at the time there were advisors of AIG that were also advising the New York Fed. Were you aware of any conflicts among these advisors or were there any discussions about what kind of conflict this might bring about?

Secretary GEITHNER. Well, when AIG came to us and started to try to walk us through their financial condition, they had advisors with them and they were also in discussion with other advisors that were not with us in the room at that time.

Mr. WESTMORELAND. When did that dollar amount become—after the discussions, at what point in time was a dollar amount derived at?

Secretary GEITHNER. You mean the initial terms of the initial loan?

Mr. WESTMORELAND. Yes, the initial——

Secretary GEITHNER. I think we reached that decision probably just on the eve of the formal agreement.

Mr. WESTMORELAND. OK.

Secretary GEITHNER. I mean, again, we were trying to do——

Mr. WESTMORELAND. And what would that date have been, do you remember that date?

Secretary GEITHNER. Well, it would have been—you know, the 16th was when we concluded this transaction, so it would have been just before that.

Mr. WESTMORELAND. Let me ask. On the counterparties, when was that meeting with the counterparties to discuss what the payment might be to them, do you remember those dates?

Secretary GEITHNER. I do not believe there was a meeting with counterparties. What I asked my colleagues to do, after looking at a range of options, is to approach the counterparties individually and try to negotiate concessions.

Mr. WESTMORELAND. So there was no actual meeting where all the counterparties were in a room and——

Secretary GEITHNER. I don't think—I would have to check the record. I would be happy to check the record and get back to you, but I do not believe that my colleagues at the New York Fed brought them in a room together.

Mr. WESTMORELAND. So when you say your colleagues, these are people that actually worked for you, they were under your direction?

Secretary GEITHNER. Absolutely. And they acted at my direction.

Mr. WESTMORELAND. Yes, sir. So you were aware of the 100 percent payment to the counterparties.

Secretary GEITHNER. As I have said many times, we decided, and I fully supported, the decision to——

Mr. WESTMORELAND. I understand. That is a yes, that you——

Secretary GEITHNER. That is a yes. I am sorry.

Mr. WESTMORELAND. OK. Now, in each one of these meetings with the counterparties to negotiate, we weren't able to negotiate any of them down?

Secretary GEITHNER. Yes. I mean, I think it is the hardest thing——

Mr. WESTMORELAND. I mean, there were separate meetings, I guess? I mean, did you question the negotiating skills of some of these people that——

Secretary GEITHNER. No. These were—again, these were very talented people with a lot of experience who knew how to do this; many had done this for a living. But, again, unless you can threaten default or threaten to pay below par—you understand this—you don't have any leverage in the transaction. And, in fact, if we had negotiated with the threat of default like that, our concern was that would risk a downgrade and would have brought about the collapse of——

Mr. WESTMORELAND. Do you know if AIG had approached any of these people about any type of negotiations about what a sum may have been? Because once the Government gets behind it, like you said, it takes way your negotiating skill.

Secretary GEITHNER. You are exactly right. You are exactly right. And I am not sure, but I think, if I am not mistaken, AIG had probably tried to do that before, before the Government came in, but I can't speak to that today.

Mr. WESTMORELAND. But these people with these credit default swaps, they were all bright people, they knew the high risk of what they were getting involved with, did they not?

Secretary GEITHNER. Well, you know, the tragic lesson of this crisis is lots of bright people with lots of experience who should have known better made bets on the future of the country that assumed house prices would never fall, and the judgments AIG made were very similar to the mistakes the rating agencies made.

Mr. WESTMORELAND. But these people were making a lot of money off of this. I mean, this was a high risk, high reward business, right?

Secretary GEITHNER. Oh, you mean the people at AIG? Oh, yes, absolutely.

Mr. WESTMORELAND. It is obvious that the AIG deal is a bad deal for the taxpayers. Is this deal being renegotiated and is anybody at the Treasury working with AIG to try to renegotiate this deal?

Secretary GEITHNER. Congressman, it is a better deal for the taxpayer than the alternatives, and is proving, in many ways, far better than many of us thought, although, as I said, the U.S. Government is still exposed to substantial risk of loss. But we have a new board in place——

Mr. WESTMORELAND. Just answer, because I have one more question.

Chairman TOWNS. No, the gentleman's time has expired and, of course, the gentleman from Maryland is recognized for 5 minutes.

Mr. VAN HOLLEN. Thank you, Mr. Chairman.

Thank you, Mr. Secretary, for your testimony.

As you indicated, the previous administration came to Congress and to the country and said we faced an extraordinary circumstance, that failure to act to help rescue the financial industry would hurt people on Main Street, innocent bystanders in this process, and you took the action that you did and you have properly said that we need to learn the lessons from what happened, and the administration and the Congress are working to do just that.

Here in the House, we already passed a Wall Street accountability bill to try to do two things: No. 1, provide the Fed and others with tools to make sure we don't have a situation where a firm becomes too big to fail in a manner that it hurts innocent people; second, to make sure that there is a failsafe, if somehow that happens, there is a pool of money raised from the banks, not from the taxpayers, to pay for the rescue; and, No. 3—and the President has proposed this—a fee on the biggest financial institutions, $50 billion plus in assets to recover every penny of TARP money. And I think it is important to understand, that everyone understands that includes every penny extended to AIG and every penny extended to the counterparties.

Now, in the House we passed a bill and we had an amendment to that bill offered by Congressman Gary Peters of Michigan. I have it right here. And it says that fee will remain on the biggest banks not just to capitalize a fund to be used in the event of future problems that they have to pay for their own, but it says you keep that fee on until you recover every penny. And I must say I was surprised—I wish all our colleagues on the other side of the aisle were here—I was surprised that this very simple idea was rejected unanimously by the other side in a vote we had on this. And that vote would have ensured—it passed, but that was a vote to make sure that we get back every penny that the taxpayer gave to AIG, every penny that the taxpayer gave to the counterparties.

So if you could just speak to the importance of making sure, No. 1, we take measures to prevent this from happening in the future, but, just as importantly, making sure we let everybody on Main

Street know that their money that they helped send to rescue the package will be recovered if we adopt the proposal in the House and the President's proposal.

Secretary GEITHNER. If Congress joins the President in adopting this proposed financial fee, then the American taxpayer will not be exposed to a penny of loss for everything the Government had to do to fix this mess in AIG or everywhere else. That is not enough, though. We believe it is very important to make sure we work with Congress to put in place constraints that will prevent this from happening again. It was a tragic failure of the country not to act sooner to limit risk-taking by some of the largest institutions in the world that were operating with not enough capital and no oversight, and we have to make it clear in the future that we are going to be able to let firms fail without costing the taxpayers money and without costing collateral damage.

Now, Mr. Van Hollen, I just want to say one thing. The cost to the American people cannot be captured in the simple financial costs of the TARP. We will protect them from those costs if Congress passes this fee, but the costs of the crisis are much more damaging. It caused much more damage. It can never be captured by the accounting costs of the losses under TARP. But we have a great responsibility and obligation to reform the system so that they are not in that position again, and the least we can do to make sure that taxpayers aren't bearing the direct costs that we took in AIG, forced to take in AIG and elsewhere.

Mr. VAN HOLLEN. Obviously, the cost of some of these bad decisions obviously went beyond [remarks off microphone] that if we adopt the amendment the House has taken as a matter of final law, or the President's proposal, which is very similar, the moneys that have been the subject of the conversation today that the taxpayers attended to AIG and that went to the counterparties, will be fully recouped and returned to the Fed Treasury on behalf of the taxpayers.

Secretary GEITHNER. That is exactly right. It is better than that, though, Congressman, because the specific transaction that is the subject of so much attention, appropriately, in this hearing, themselves are likely to earn the taxpayer a modest profit. The Government is still exposed to some risk of loss on the rest of its investments, but if we adopt this fee the taxpayers will not bear a penny of that cost.

Mr. VAN HOLLEN. Thank you, Mr. Secretary.

Mr. WELCH [presiding]. The Chair recognizes Mr. McHenry.

Mr. MCHENRY. Just to be clear, there is $68 billion worth of loss, $30.4 billion associated with this AIG deal we are talking about now, so there is significant loss to the taxpayers already through TARP. So this new tax is simply about making up for that revenue.

Mr. Secretary, do you support H.R. 4173, the Wall Street Reform and Consumer Protection Act?

Secretary GEITHNER. Congressman, I am not sure of the precise legislative amendment you are citing. Can you describe the bill?

Mr. MCHENRY. No, it is not an amendment, it is a bill sponsored by Barney Frank of Massachusetts.

Secretary GEITHNER. Is this the comprehensive financial reform law that passed the House in December?

Mr. MCHENRY. Yes.

Secretary GEITHNER. Yes, I support that.

Mr. MCHENRY. You support that. And do you support the Volcker rule?

Secretary GEITHNER. Absolutely. What the President proposed is that working with the bill that passed the House, which included a provision that I think Mr. Kanjorski authored, to give the Government the ability to limit risk-taking by banks, that we make sure those translate into limits that will actually prevent risk-taking in the future.

Mr. MCHENRY. So it is consistent with H.R. 4173?

Secretary GEITHNER. Absolutely. That bill—and this is very important for people to understand. That bill included a provision——

Mr. MCHENRY. I understand; I am on the committee.

Secretary GEITHNER. Yes—included a provision that would give the Government the ability to limit risk-taking in a way to help prevent future crises.

Mr. MCHENRY. Wasn't it your legislative staff that really worked to change the Kanjorski amendment?

Secretary GEITHNER. Well, again, we worked closely with members of that committee on a whole range of those provisions to make sure that they met the intent——

Mr. MCHENRY. No, you are not answering my question.

Secretary GEITHNER. Oh, on that amendment? Absolutely we worked with them on that amendment.

Mr. MCHENRY. You worked with them on that amendment——

Secretary GEITHNER. But on alternate——

Mr. MCHENRY [continuing]. To limit it in terms of its reach?

Secretary GEITHNER. No. We worked on it to limit it to make sure that it was going to work.

Mr. MCHENRY. OK, let's not—OK. So, in essence, the Volcker rule is something you support?

Secretary GEITHNER. Yes.

Mr. MCHENRY. OK. You testified last month before the Joint Economic Committee, "I would not support reinstating Glass-Steagall, and I don't actually believe that the end of Glass-Steagall played a significant role in the cause of this crisis." Do you still stand by that statement?

Secretary GEITHNER. Absolutely.

Mr. MCHENRY. How do you reconcile that belief with this rule that, in essence, limits or forces banks to divest in hedge funds and private equity and all these other additional elements that is in essence Glass-Steagall?

Secretary GEITHNER. Well, what Glass-Steagall did was to allow banks to underwrite equities and to engage in a whole range of other types of financial activities, insurance as well——

Mr. MCHENRY. It limited that ability, to be clear.

Secretary GEITHNER. And we support, as I think the bill that you cited did support, it did actually provide authority to limit a set of activities so that the access to the safety net is not subsidizing excessive risk-taking. It is a simple principle. Does it dial back some of the Graham-Leach power reforms? It does do that.

Mr. MCHENRY. OK. So——

Secretary GEITHNER. But it is not what people typically referred to as Glass-Steagall.

Mr. MCHENRY. OK, so it also says that if you engage in a certain type of—if you have a certain form, meaning a bank holding company, you have to adhere to certain rules, correct?

Secretary GEITHNER. That is right.

Mr. MCHENRY. OK. You also testified before the Financial Services Committee, of which I sit, last year that "Financial products and institutions should be regulated by the economic function they provide and the risks they present, not the legal form they take."

Secretary GEITHNER. That is right, I agree with that.

Mr. MCHENRY. And so you support a rule that says, based on a legal form you take, you have to adhere to these principles. How do you reconcile this?

Secretary GEITHNER. They are perfectly consistent, but let me state the basic principle again.

Mr. MCHENRY. They are perfectly opposites.

Secretary GEITHNER. No. What we are saying is—and this is very important for people to understand. If you are operating in the financial markets, you are helping companies raise credit, raise capital, you are helping make markets work, you are providing liquidity to markets, it doesn't matter, it shouldn't matter to us or the American people whether you are called Goldman Sachs or whether you are called JP Morgan. You should be subjected to a set of constraints on capital, on leverage and how you are funded that limit the amount of risks you take.

If, in addition to that, you want to own a bank and operate a bank, then there are a set of other limits that we think are good in the public interest so that, again, you can't take advantage of that access to the safety net to subsidize a set of activities that are not essential to——

Mr. MCHENRY. But basically you are saying, if you just simply drop the bank holding company label, you are out from under this regulation.

Secretary GEITHNER. Absolutely not. And that would be a mistake for the country. Our view is——

Mr. MCHENRY. That is actually what the one-page rule——

Secretary GEITHNER. No, it does not do that. That is not a fair reading of the rule. But, Congressman, maybe this would be helpful for me to say to you. We will work very closely with Members on both sides of the aisle to make sure that this legislation results in a set of sensible constraints in risk-taking——

Mr. MCHENRY. That would be something new——

Mr. WELCH. The gentleman's time has expired.

Mr. MCHENRY [continuing]. Over the last 13 months, because you have not reached out to Republicans, to be clear, on the Financial Services Committee.

Secretary GEITHNER. That is not true, but, again, I am happy, going forward, to make sure that, as we try to give these force of law, reflect them in regulation, we do so carefully, with full consultation.

Mr. WELCH. The gentleman's time has expired and the chairman recognizes himself for 5 minutes.

Thank you, Mr. Geithner, for being here. No. 1, I just want to remind my colleagues on both sides that the whole request for the bailout that had to be administered by the Treasury Department was at the request of then President Bush. And, second, I understand your testimony that the people responsible for administering this made the best decisions they could under the circumstances.

I just want to ask a couple of questions, though, that start with one of the statements you made, Mr. Geithner, about the effect of the actions taken has stabilized the financial system. I am not here to argue that. The question I have is has it helped the broad Main Street economy. And there are many who believe, and I am among them, that Wall Street got out ahead of itself, got in the business of self-enrichment rather than financing American jobs, American entrepreneurs, and actually transformed itself from an entity that was about creating jobs into the greatest job killing machine in the history of the country.

There are two things that I want to ask. One is the bank fee that President Obama has endorsed, you see that as essential to have the folks who were largely responsible for the financial meltdown pay the cost so that it is not the taxpayers, is that correct?

Secretary GEITHNER. Absolutely. In the reforms we proposed to the Congress back in June, at the center of that proposal was a basic principle which, in the future, governments exposed to risk of loss, the banks pay. In the TARP legislation you referred to, there is an explicit provision there that puts an obligation on me to propose ways to recoup the costs, and we propose that in the President's financial responsibility bill.

Mr. WELCH. All right, thank you. And I support that; I am glad you are doing it.

Second, there are a number of us, well over 60, that are supporting a tax on Wall Street bonuses, and I just want to get your opinion on this; and I will give an example of the kind of conduct that was allowed to occur. It has been reported, as you know, in the New York Times that Goldman Sachs had a department that bundled subprime mortgages. It then had folks who advocated to the rating agencies to give it the highest rating possible. It then went to its trusted clients and sold those, and then it went to its trading desk and sold them short.

Is that the type of conduct that you think should be monitored and curbed by any financial regulatory monitor?

Secretary GEITHNER. Congressman, I believe deeply that we need tougher rules, enforced more effectively and evenly to make sure that consumers and investors are not taken advantage of, and the system is not so fragile the Government has to step in in the future and take this enormous risk of loss. I deeply believe that.

Mr. WELCH. Let me get to—let me just ask you about the bonus tax, because I would be interested in this. Firms like Goldman received TARP funds. They received low interest money from the open window of the Federal Reserve and, of course, Goldman and other firms received direct pass-through payments when AIG was bailed out, correct?

And when Mr. Paulson, your predecessor, was on the phone requesting this money—this was not anything that you made the request for—he assured us that Wall Street had learned its ways.

Goldman and the other Wall Street firms are back to their old ways; they have been so successful—and let's give them credit, they are good at what they do. The question is whether what they do is good for the economy and for Main Street. They have been able to set aside $140 billion to $160 billion for bonuses. And they could have lent that out, they could have added to their capital base, and the third choice was they could put it in their pockets, which is the one they have chosen.

Do you think, in view of the fact that much of their profit was made through taxpayer generosity, it would be appropriate to tax bonuses, as I suggest in my legislation, at 50 percent above $50,000?

Secretary GEITHNER. Congressman, of course I would be happy to take a careful look at that legislation and talk to you about how best to deal with that. The basic principle that we support fully is to make sure that the American taxpayer is not exposed to a penny of losses from the actions the Government had to take under the TARP authority; and I completely agree, as I said earlier, that we need to work with the Congress to make sure we bring about fundamental changes in how bankers are paid so that they are not taking risks that could imperil the economy as a whole. Doing that is hard to do right. We have tried in the past, not very successfully. It is an obligation that the shareholders have and boards have too, but it is the Government's responsibility in the end to make sure——

Mr. WELCH. My time is almost up. We would take the money that was raised from that and put it into small business lending, and, as you know, the big banks that received TARP funds have reduced lending to American enterprise. Folks in Vermont who run businesses ask me, if those guys make so much money, how come they can't lend me any?

Secretary GEITHNER. I agree. And I think if you saw the paper today, we are close to proposing to the Congress that we take a large amount of the resources that we have gotten back from banks, from the large banks, and devote them to exactly that objective, trying to make sure that small banks and small businesses have access to credit.

Mr. WELCH. Thank you, Mr. Secretary. My time is up.

The Chair now recognizes the gentleman from Ohio, Mr. Jordan.

Mr. JORDAN. Thank you, Mr. Chairman.

Thank you, Mr. Secretary, for being with us today. Now, Mr. Secretary, you were involved—you have said this many times—involved with the decision 15, 18 months ago relative to the initial TARP bailout. You were involved in all that; you thought it was the right decision to make at the time, coming to Congress, asking for the $700 billion?

Secretary GEITHNER. Oh, I thought it was absolutely essential at that point. The country had no choice.

Mr. JORDAN. And this committee has had several hearings on the Bank of America and Merrill Lynch, and you were involved in that decision. We have emails that talked about you were in the loop, you knew what was going on there; you were supportive of what took place with the merger of—with the acquisition of Merrill by Bank of America. Yes or no?

Secretary GEITHNER. Well, that is right that, at that time, I was part of an effort to try to find the solution, private solution to Merrill Lynch at that point, and I thought that action at the time was necessary and appropriate, yes.

Mr. JORDAN. And today you have said that you think the initial decision relative to AIG and the payment to the counterparties, you think that was appropriate. You stated that strongly in your written testimony. You talk about this is in the best interest of the American people.

Secretary GEITHNER. I do. I do.

Mr. JORDAN. We did not act to help form banks, we acted because the consequences of failing at that time, in those circumstances, would have been catastrophic to our economy, American families, and American businesses. You think it was definitely the right decision?

Secretary GEITHNER. I do.

Mr. JORDAN. And the staff that worked for you at the New York Fed would be in agreement with that analysis, that this was so critical, this had to get done, the sky was going to fall, the world was going to end if we did not do what you decided to do relative to the counterparties and the $62 billion that was spent, is that correct?

Secretary GEITHNER. I believe it is. But I think it would be fair to say there were those among us involved in this in each of the industries involved—Washington, New York Treasury—who were deeply troubled by that choice, were not comfortable with this——

Mr. JORDAN. Were not comfortable with it, but you thought it was what you had to do at the time.

Secretary GEITHNER. I believe that, yes.

Mr. JORDAN. And it was so important, as you have said in your written and your testimony here this morning, your oral testimony, that, you know, this was critical to American families, American businesses.

Secretary GEITHNER. I believe that.

Mr. JORDAN. So it begs the obvious question: Why the secrecy relative to disclosure? If it is that important, $62 billion, why in the heck not disclose it when it is happening, since you have subsequently done that? Why the secrecy? And, frankly, why weren't you—if it is that critical, if it is that important, why in the heck did you recuse yourself? Why weren't you involved?

Secretary GEITHNER. Well, again, just to step back a second, when the Fed disclosed this in March 2009, I thought it was the right thing to do, and I think reasonable people, looking back at this, could say why wasn't that possible sooner. I think that is a reasonable question——

Mr. JORDAN. Why wasn't it possible in November when it was all going down?

Secretary GEITHNER. Right. But all I can say is what I understand and was involved in, and I was not involved in discussions about decisions about what to do with that particular transaction, the counterparties, or the details. And that is because of decisions——

Mr. JORDAN. Let me ask you this. Do you believe the decision that was made by the folks who worked for you at the New York

Fed to not disclose until March and not disclose when it was all taking place, do you support that decision?

Secretary GEITHNER. Congressman, I, as I said——

Mr. JORDAN. It is a yes or no. I mean, you have said you are transparency; you said this was so critical, the world was going to end, everything was going to go to——

Secretary GEITHNER. Let me tell you something I——

Mr. JORDAN. Why not?

Secretary GEITHNER. Let me tell you something I deeply believe, OK? It is very hard to put yourself in shoes you did not occupy and have really a fair sense to evaluate those actions in that case. And I don't feel like I can put myself in their shoes at that time.

Mr. JORDAN. Let me tell you what I think happened.

Secretary GEITHNER. But I do believe that they acted with great integrity, care, and judgment after——

Mr. JORDAN. Here is what happened. Here is what happened. Mr. Lynch was on the right trail over here. I mean, this is a pattern, we have seen it. You came to the Congress of the United States, you said give us $700 billion of taxpayer money.

Secretary GEITHNER. I did not do that.

Mr. JORDAN. I am saying the Government. The Government came to the Congress, give us——

Secretary GEITHNER. Your Government, your President at that time.

Mr. JORDAN. I understand. I didn't say Democrat or Republican. I understand the Government. Give us the money, we are going to go buy the troubled assets. They didn't do that. Nine days later, 10 days later, as Mr. Lynch pointed out, you were in the room when they told the nine biggest banks we are not going to buy the troubled assets, you are going to take the TARP money.

Secretary GEITHNER. I was, and that was one of the best decisions, one of the most important decisions that——

Mr. JORDAN. But understand the pattern. The Congress of the United States was told one thing; 10 days later an entirely different action was taking place.

Secretary GEITHNER. I don't think that is actually correct. What the Congress authorized was the billions——

Mr. JORDAN. You don't think the Congress passed that bill because they understood that the money that the taxpayers were going to put up was going to be used to buy troubled assets?

Secretary GEITHNER. Well, as I said, I can't put myself in your shoes, but I think the salient point is that the authority that President Bush asked for gave my predecessor the authority to put capital in banks, and doing that——

Mr. JORDAN. Here is the pattern, Mr. Geithner. Mr. Secretary, here is the pattern. The Government comes to the taxpayer, says we need more of your money, we need a boatload of your money, the world is going to end; we want it for a specific purpose; then they do it for something else. Then they come to the taxpayers and say we need more of your money and we are going to use $62 billion and they don't disclose to the taxpayer what is going on. This is why we never should have traveled down this road, this unprecedented involvement by the Government in the private sector. We have seen it——

Mr. WELCH. The gentleman's time has expired.

Mr. JORDAN. We have seen it with Bank of America and Merrill Lynch, we have seen it now with AIG.

I thank the chairman.

Mr. WELCH. The gentleman's time has expired. Thank you.

The Chair recognizes Mr. Clay.

Mr. CLAY. Thank you so much, Mr. Chairman. I want to thank Chairman Towns and Mr. Issa for conducting this hearing.

Secretary Geithner, several economists and policymakers assert that AIG's ability to provide cash collateral to their counterparties was not relevant in designing their assistance package. What is your opinion on this claim that it was not relevant in designing the assistance?

Secretary GEITHNER. I agree with that. What was relevant and necessary was how to restructure this firm in ways to protect the taxpayer, to the extent we could, from the risk of greater losses, and our choice was at this point this very stark, tragic choice, which is to let AIG default or not. And we thought that default itself would have been much more expensive.

Mr. CLAY. OK, help me and help the American people understand. Why was AIG's ability to make payments to its counterparties for their toxic assets even a factor in determining the amount of bailout money to award them?

Secretary GEITHNER. For an insurance company or any financial institution to operate, they need to be able to operate with a high credit rating. Without that, they could not borrow money to function. They could not write insurance contracts because people would not believe they would have the financial wherewithal to back those commitments.

So the rating is critical. If we were to have defaulted on any of those legal contracts, AIG would have been downgraded. The counterparties would have the right to take more money and to default on and to bring about the basic collapse of the firm. So it is that stark, tragic choice. If AIG had not paid, they would have lost the rating and the firm would have collapsed. If we had continued to lend them money for them to make those payments, the rating would have also been in jeopardy, because AIG already had a lot of debt at that point. So the choice was, again, to restructure them so that we limited the drain of cash and left the taxpayer with any potential positive return on those underlying securities.

Mr. CLAY. So you are saying that the counterparties would have had a right, through bankruptcy——

Secretary GEITHNER. A legal right to sue to recoup that claim.

Mr. CLAY. OK. Did anyone involved in the concession negotiations ever suggest that AIG's counterparties should not be relevant in their bailout package? Did that issue ever arise among the negotiations or anyone that you encountered during the negotiations?

Secretary GEITHNER. That is a complicated question, good question, but as I tried to explain in the testimony, what we were guided by, what was going to be the best way at least cost to prevent default and protect the system, and the entire system was at stake then, and no firm in the country would have been insulated fully from the collapse of the entire American financial system, and our judgment was that AIG's default would have materially raised the probability of that broader collapse. So, again, our choices were terrible choices, but they came down to what was the best way to prevent that outcome on the best terms for the taxpayer.

Mr. CLAY. OK, so then that gets to the point of being too big to fail. AIG's tentacles were that widespread throughout the country and the world that——

Secretary GEITHNER. It is exactly the right question. There are two things that mattered in this case. One is you had a set of firms like AIG, huge, risky, spread everywhere, involved in a whole range of things, and you had a world that was burning. So, again, the first time since the Great Depression, you had financial systems around the world really at the brink of stopping in their tracks.

And it is those two conditions that are most risky. If the world had been stable, everything had been fine, we weren't on the edge of the worst recession in generations, then we could have afforded to be completely indifferent to the fate of AIG or all those institutions. But because AIG was so large and so interconnected, and because the system was so fragile, it would have been irresponsible to take the risk, the failure would have dramatically amplified the pressures that we are still living with today.

Mr. CLAY. Could you help describe what the reaction was in negotiations to the counterparties, pros and cons, as far as, you know, paying counterparties?

Secretary GEITHNER. Again, we wrestled with lots of choices, as I tried to explain in my written testimony. We thought about whether it was better to default, to impose a haircut, to negotiate concessions under the threat of default. We thought about keep paying and watching that money keep running out the door, with the counterparties still holding the underlying assets.

We thought about negotiating over time, trying to stretch it out, see if we could find a better way to solve that problem. None of those options were realistic; none of them were feasible. They were not better than the choice we chose. And, again, I think if you look back and you take a fair reading of this, although the Government is still exposed to substantial risk of loss, those losses are much lower today because of the actions we took in AIG, and this transaction, which, again, people are so understandably concerned about, has put the taxpayer in a better position than if simply we kept making those payments or if we defaulted on them.

Mr. CLAY. Thank you, Mr. Secretary, for your responses.

Chairman TOWNS. The gentleman's time has expired.

I now yield 5 minutes to the gentleman from California, Congressman Bilbray.

Mr. BILBRAY. Thank you.

Mr. Secretary, we are supposed to do oversight and reform, so we are trying to get the information so that we can do the reform to make sure the next time this process comes up we have procedures and laws that address this. So it is real important that we identify how this went so we can try to correct it and make sure it doesn't happen again. Not only in March you knew that there was a so-called disclosure issue, but in February you had said, in a speech, that one of the major issues that you were concerned about is the lack of disclosure that was causing the American people not to trust the system.

Now, I think we all agree that in layman's terms, with the average citizen, when they heard disclosure issue, they hear cover-up. Now, why, in a system that is supposed to be open—the American people have a right to know where their money goes. Why was there even a disclosure issue? Why were we even discussing the so-called cover-up of the $160 billion, where it was going, in this process?

Why was that even an issue that as soon as you knew that there was a problem there, that somebody didn't clarify this? Was that your staff had basically did not inform you that there had been this cover-up, this disclosure issue, and did you make that decision or was that decision made outside? Because AIG sent the information over; it was an internal process within the Government itself that said we are not going to disclose to the public this information.

Secretary GEITHNER. My colleagues at the New York Fed I think have put in the public domain a very thoughtful explanation of the judgments they wrestled with and ultimately reached, and I know, and I am confident, that their colleagues in Washington spent a huge amount of time throughout those months trying to wrestle with how to meet the understandable public interest in greater disclosure of these things, and they ultimately, I think appropriately, came to the decision that they could and should put that information in the public domain.

Now, you are exactly right, I have been a great proponent of greater transparency, and the centerpiece of the strategy that we adopted to fix this mess in the financial system was to force the largest banks in the country to disclose for the first time to the public, to all investors, the scale of losses they might face in the event this recession was much more damaging than it proved to be, and that provided the basis for private investors judging who was strong, who was less strong, and deciding to put capital into those institutions.

Mr. BILBRAY. In other words, did your staff know the cover-up was there, a disclosure issue was there before you knew it was there? Was the decision to——

Secretary GEITHNER. Again, I don't—I think, again, as the record the committee has already put in shows, there were discussions that were happening about what to disclose when throughout that period of time, but——

Mr. BILBRAY. Were you involved in those discussions?

Secretary GEITHNER. As I said in my thing, I will say it again, I played no role in decisions about what to disclose about these transactions to these individual counterparties.

Mr. BILBRAY. Did your staff make the decision not to inform you or include you in that decisionmaking process?

Secretary GEITHNER. Yes, they did, although I made the decision——

Mr. BILBRAY. Would you want to know about that or would you prefer that you didn't know about it at the time?

Secretary GEITHNER. I think, in retrospect, I wish I had known, frankly. But after November 24th I appropriately removed myself from decisions about a whole range of policy issues the Fed was dealing with. But the people that were making those decisions, in close consultation with people in Washington and with legal counsel, are people of great judgment, enormous integrity, and I have enormous trust and confidence not just in their judgment, but in the quality of the decisions they made throughout that period of time.

Mr. BILBRAY. Do you feel today that at the time that they made the decision to do the cover-up, the disclosure issue, that they felt you did not want to know about it at the time? Do you think they made a decision that——

Secretary GEITHNER. I do not—in my entire time there, I was never aware of a situation in which my colleagues sought to shield me from something consequential. I was president of the New York Fed; I was going to be accountable for decisions made on my watch. But after the 24th, for reasons that I think are fair and right for the institution, I could no longer run those day-to-day judgments, and I withdrew from those and I think those were necessary. Now——

Mr. BILBRAY. And your staff decided to shield you from the cover-up side of it too?

Secretary GEITHNER. No, no. I decided that I would withdraw myself from—I didn't decide this alone, I decided this in consultation with the chairman of the board of Governors of the Federal Reserve System and with the incoming administration to protect the institution from the unique condition I was in then.

Mr. BILBRAY. Mr. Secretary, what date did you know that there was a cover-up, a disclosure issue? When were you informed?

Secretary GEITHNER. I only knew about these discussions about disclosure when they started to be in the public domain. I actually don't know when they first rose to the attention of the Congress, but when they rose to the attention of the Congress and they were in the press, then I was aware of it.

Chairman TOWNS. The gentleman's time has expired.

Mr. BILBRAY. Thank you very much.

Chairman TOWNS. Let me thank you, Secretary Geithner, for your testimony and, of course, we will now——

Mr. ISSA. Mr. Chairman, I would ask unanimous consent that all Members be allowed to put their questions in writing to the Secretary and would ask that the Secretary, if he would respond to them in writing, since so many Members have not been able to ask their questions.

Chairman TOWNS. Without objection, so ordered.

Thank you, Mr. Chairman.

Mr. CHAFFETZ. Mr. Chairman, I am not sure what the right point of order here is, but I recognize how tremendously busy the Secretary is, but I also recognize the need for this Congress and people on both sides of the aisle to be able to ask some questions. We have been waiting patiently here all day. I would hope that the chairman would——

Chairman TOWNS. Let me just say what the problem is. I am one—as you know, you have been here long enough now to really know me—who believes in openness and I believe in going as long as it takes. But Mr. Paulson has a problem with his schedule in terms of the amount of time that he would be allowed.

If we continue, then he will not be able to testify. That is the issue that we have to deal with. So, that is the reason why we are cutting it, and it was agreed that this would happen. And, of course, I understand there are several people that did not have an opportunity to raise questions, but what I would suggest is that you put the questions to the Secretary in writing and he will answer, because, if not, then the second witness we will not be able to hear from at all, and I think that would be——

Mr. CHAFFETZ. Mr. Chairman, if I could be so bold, my guess is, if we were to survey or talk to the people on the panel, particularly people who haven't had a chance to ask questions, I think, with all due respect, we would much rather hear from the current Treasury Secretary than the past Treasury Secretary, whose schedule is probably a little bit more flexible than the current Treasury Secretary.

Chairman TOWNS. I understand that, but the point of the matter is that we have a hearing that has been scheduled and, of course, has been structured. I wish we could stay here and allow everybody to do that, but the point is that I think in this situation——

Mr. CHAFFETZ. Mr. Chairman.

Chairman TOWNS. I would be delighted to yield to the gentleman again, yes.

Mr. CHAFFETZ. And I appreciate it, because you have always been so fair and very generous, and personally very good to me. Is there a way that we could vote on which direction to go on this?

Chairman TOWNS. Well, you know, it is actually up to the chairman, but let me say what I would like to do. I would give a minute to two on this side and a minute to two on this side, and that is it. I mean, we have to move forward. We have a scheduled hearing that is here looking for certain information——

Mr. KUCINICH. Would the gentleman yield?

Chairman TOWNS [continuing]. Looking for certain information. In order to get the information, we need to talk to the present Secretary, we need to talk to the past, and, of course, we have others that we still want to——

Mr. KUCINICH. Would the gentleman yield?

Mr. FORTENBERRY. Mr. Chairman, I join with you in that unanimous consent for 2 additional minutes per side equally divided.

Mr. KUCINICH. Reserving the right to object. Mr. Chairman, I just want to say that any member of this committee has the ability to submit questions in writing. Mr. Geithner, in response to an earlier question, said that, in the interest of time, that he would be willing to answer questions in writing. Is that not true, Mr. Geithner?

Secretary GEITHNER. Absolutely. Of course.

Mr. KUCINICH. OK. So, Mr. Chairman, anybody who wouldn't get a chance to ask a question here can still put it in writing. I withdraw any objection.

Chairman TOWNS. Let me just say that we will go two on this side, two on that side, but a minute, remember.

Mr. FORTENBERRY. Mr. Chairman, reserving the right to object.

Chairman TOWNS. I don't know what you are objecting to.

Mr. FORTENBERRY. If you would recognize me. The unanimous consent request for 2 minutes each. I would be happy, Mr. Chairman, to forego my time with Secretary Paulson to ask Secretary Geithner——

Chairman TOWNS. Well, I wish we could operate that way, but, you know, when you have hearings that are structured, they are not structured in the fact that someone would give up their time. I mean, that is not the way we do it. So the point of the matter is that we either accept the 2-minutes on each side or we move forward. OK? So that is what is on the table—2 minutes on this side, 2 minutes on that side.

Mr. FORTENBERRY. I withdraw my objection.

Chairman TOWNS. Designate the two on this side.

Mr. Connolly, you have a minute to raise one question with the Secretary. Mr. Connolly from Virginia.

Mr. CONNOLLY. Thank you, Mr. Chairman.

Chairman TOWNS. Recognized for 1 minute.

Mr. CONNOLLY. Thank you, Mr. Chairman.

Mr. Geithner, we only have 1 minute. One has the sense that some people in this room perhaps want to rewrite history, and I understand, given the history, why they might want to do that. In your opening statement you talked about the need for financial regulatory reform. Could you expand on why we need that, particularly when it comes to regulating that which was resisted from regulation in the past, like derivatives and credit default swaps?

Secretary GEITHNER. I don't think it is a hard case to make. I think you just have to look at the wreckage caused by the crisis to say the system failed dramatically. And, again, the two most simple failures that happened is people were allowed to take risk without constraints. We let a system operate where institutions that were huge and consequential operated with no adult supervision, with no constraints, and they brought the country to the edge of collapse.

Let me just say one thing in common with the following firms. Fannie and Freddie, the largest investment banks in the country; AIG, a set of specialized insurance companies, a whole range of consumer finance companies, a bunch of thrifts. They all had one thing in common, which is they were not subject to a set of sensible rules to constrain the risks they could take.

What we propose in financial reform is to change that. It is a simple imperative. That is not enough though, because people will make mistakes in the future. So we need to make sure, when they make those mistakes, that we can let them fail and failure can happen without catastrophic damage. We need to be able to contain the damage, isolate it, draw a line around it, put them out of their misery, put them out of existence without the taxpayer being exposed; and we need to make sure that we don't have a system where the taxpayer is exposed to the risk of loss or that investors and creditors live with the expectation the Government will be there again.

And, again, that is something that I think we all have a huge obligation and responsibility. It was the laws of the land that allowed that to happen, the laws of the land that made it impossible for the Government to act, and I think we need to work together to change that.

Mr. CONNOLLY. I thank the gentleman and I thank the chairman for his consideration.

Chairman TOWNS. Thank you very much.

I now recognize Mr. Fortenberry for 1 minute.

Mr. FORTENBERRY. Thank you, Mr. Chairman.

Mr. Secretary, welcome. For the last year and a half we have been privatizing profits and socializing risk, and if the optics on the AIG aren't bad enough, the counterparties to the AIG, who received 100 parity for their liabilities, 7 of the top 10 are foreign firms. Societe Generale was the top recipient of $16.5 billion of American taxpayer bailouts, in effect, followed by Goldman Sachs.

Now, you said this economy is in crisis. This year, Goldman Sachs will give $16 billion of bonus payments, about $500,000 per employee. This is really difficult to understand why there wasn't, at first, a desire to have transparency in regards to counterparty transactions. Would you address that, please?

Secretary GEITHNER. Oh, I am not sure if you were here for that part of the conversation.

Mr. FORTENBERRY. I have been here the entire time.

Secretary GEITHNER. OK.

Mr. FORTENBERRY. Except for votes.

Secretary GEITHNER. But, again, the actions we took were necessary in the public interest, better than the alternatives, to help prevent catastrophic damage. And if you are outraged, as I think you should be, about how the economy and our system was in this mess, I hope you will join with us in trying to work to make sure it doesn't happen in the future. This is not something that should be Republican or Democrat.

There is a deep, I think moral, obligation we have to try to make sure that we put in place reforms that will prevent this from happening again. If the Government had done that sooner, this would have been less damaging. And a critical part of the failure was we ran a country, largest economy in the world, largest financial system in the world, without having the kind of bankruptcy type powers we had for banks for decades. And that is something that——

Mr. FORTENBERRY. Let's try to do that on a bipartisan basis, sir, please. But you understand why——

Chairman TOWNS. I am sorry, the gentleman's time has expired.

Now I recognize the gentleman from Illinois, Congressman Davis, for 1 minute.

Mr. DAVIS. Thank you very much, Mr. Chairman.

Thank you, Mr. Secretary. Let me just ask if you had to do it again, to do it all over, would you change any of the decisions that you made in the fall of 2008 to rescue AIG and pay the counterparties par?

Secretary GEITHNER. Congressman, again, I think about this a lot, and one of the great strengths of our country is, again, people have to look back and come to their own judgment whether we made the best choices. But I am very confident that we made the best of a set of terrible choices; that there were no better alternatives. We did not have the option of bankruptcy; we did not have the option of defaults; we did not have the option of selective haircuts. It would have been catastrophic to let the institution fail. We didn't rescue AIG; we intervened so that we could dismember it safely, without it wrecking the country and the system.

I think the big mistakes we made as a country, and they are mistakes that we have to reflect on deeply for a long time, were why the Government didn't act sooner to limit risk-taking, why the Government didn't provide competent authorities the ability to contain risk-taking, and why didn't we have in place the kind of tools we have had for a long time for banks to try to deal with these kinds of failures. I think those were tragic mistakes.

The lesson of financial crises is if you don't act sooner, things get to the point where they can cause catastrophic damage; and if you let it, if you stand back and hope it will burn itself out, correct itself, it will be a good, healthy adjustment for the economy, that can cause enormous damage, and it will cause enormous damage not just to the American lives and people will be living with for a long time, but to the revenue base of the country, deeply impairs the capacity for Government to do things that are necessary like we need resources for, protect national security, make sure teachers can be in the schools. These things are deeply connected. If you stand back and try to hope the market will fix itself, you court catastrophe. I hope we learned that lesson. It should never happen again.

Chairman TOWNS. Thank you very much. The gentleman's time has expired.

I now recognize the gentleman from Utah, Mr. Chaffetz.

Mr. CHAFFETZ. Thank you, Mr. Chairman.

Thank you, Mr. Secretary. I was going to ask about the 18 phone calls you made to Rahm Emanuel, more than any other Member of Congress, but we will have to save that for another day. What I would like to ask you about is this idea that they are going to make profits. I am going to read two statements and ask you a question, from Neil Barofsky's testimony that is coming up.

First one is, on page 13, "Treasury's own TARP financial statement estimates that Treasury will not be made whole, but is rather projected to lose more than $30 billion on its AIG investments."

Second quote, later in the same paragraph, "Narrowly asserting that taxpayers will be "made whole" on Maiden Lane III—just one part of the AIG counterparty transactions—without mentioning the huge losses Treasury expects to suffer on other, inextricably linked parts of the very same transactions is simply unacceptable; the American people deserve better."

So my question, and I am hoping that you can respond to those two statements, is when you refer to profits from the AIG counterparty bailout, are you counting the cost of the $35 billion in cash AIG handed over to the counterparties or just the $27 billion they got directly from the New York Fed?

Secretary GEITHNER. Congressman, I think that Mr. Barofsky and I actually agree on this, and I said in my statement—I was very clear—the Government is still exposed to substantial risk of loss on its investments in AIG. The Federal Reserve in this transaction, I think more generally, is unlikely to face any loss. That is a good thing. We should welcome that.

But the Government is still exposed to risk of loss. We don't know how large those losses will be. What we refer to is not a projection, it is just an estimate based on current market prices. But the really important thing—and I hope you will join us in this—is if we adopt this financial responsibility fee, the taxpayer will not bear a penny of the burden for what we did——

Mr. CHAFFETZ. Sounds like a tax to me. It doesn't sound——

Secretary GEITHNER [continuing]. Under the TARP.

Mr. CHAFFETZ. Sounds like a tax to me.

Secretary GEITHNER. Well, you can call it what you want, but what it is is a principal.

Mr. CHAFFETZ. I call it a tax, and I wish you would too. I call it what it is.

Secretary GEITHNER. Well, again, in the law that Congress passed authorizing these actions, Congress required the Secretary of the Treasury to propose a way to make sure taxpayers are held harmless. We did that. I hope you will join us in supporting that because there is no reason why the American taxpayer should be exposed to a penny of loss in what we did in AIG. We can make that possible.

Chairman TOWNS. The gentleman's time has expired.

Thank you very much for your testimony, Mr. Secretary, and, of course, you may be excused.

Now we call upon our second panel.

[Pause.]

Chairman TOWNS. The second witness for today's hearing is former Treasury Secretary under the Bush administration, Secretary Henry Paulson.

Mr. Paulson, please stand as I administer the oath.

[Witness sworn.]

Chairman TOWNS. You may be seated.

Let the record reflect that he answered in the affirmative.

I will ask the witness to summarize his testimony in 5 minutes. Of course, we know the procedure; the yellow light means you have a minute left and the red light means stop. Then, of course, we will have time to raise questions with you. You know the procedure; you have been through this quite a few times, so good to have you back.

STATEMENT OF HENRY M. PAULSON, JR., FORMER SECRETARY, U.S. DEPARTMENT OF THE TREASURY

Mr. PAULSON. Mr. Chairman, thank you, and I will go through this quickly.

First of all, Chairman Towns, Ranking Member Issa, and distinguished members of the committee, I appreciate the invitation to testify before this committee. I was Secretary of the Treasury in 2008. In that role, I had the privilege to work with many talented men and women in Government and the private sector who labored to pull our Nation back from the brink of disaster.

The decision to rescue AIG was correct, and I strongly supported it. An AIG failure would have been devastating to the financial system and to the economy. Today's hearing relates the payments to AIG's credit default counterparties. I was not involved in any of the decisions made with respect to those payments, nor was I involved in any of the decisions about AIG's public disclosure of those payments. Those matters were handled by the Federal Reserve Bank of New York and the Federal Reserve Board. They sought to make appropriate decisions on those matters and I am confident that this review will show that they did.

I have limited knowledge on the topics of immediate interest to the committee, but I will share the following observations.

The rescue of AIG was necessary and I believe that we in the Government who acted to rescue it, including Secretary Geithner, Chairman Bernanke, and me, acted properly and in the best interest of our country. The reasons the rescue of AIG was necessary are well worth examining. I believe they are representative of the causes of other aspects of the crisis and indicate where regulatory reform is necessary.

There are three reasons we needed to save AIG that stand out in my mind. First, AIG was incredibly large and interconnected. It had a $1 trillion balance sheet, a massive derivatives business that connected it to hundreds of financial institutions, businesses, and governments; tens of millions of life insurance customers; and tens of billions of dollars of contracts guaranteeing the retirement savings of individuals. If AIG collapsed, it would have buckled our financial system and wrought economic havoc on the lives of millions of our citizens.

Second, AIG was seriously underregulated. Although many of AIG's subsidiaries, including its insurance companies, were subject to varying levels of regulation, the parent entity was, for all practical purposes, an unregulated holding company. Consequently, there was no single regulator with a complete picture of AIG or a comprehensive understanding of how it was run. It was not until AIG started to fail that regulators began to understand how badly managed it had been and how much the toxic aspects of parts of its business had infected otherwise healthy parts.

Third, AIG could not be effectively wound down. Unlike failed depository institutions, which can be taken over by the FDIC with little or no harm to depositors, or the GSEs, which were seamlessly placed into conservatorship by Treasury and the Federal Housing Finance Agency, there was and is no resolution authority available to wind down a failing institution like AIG. The only option is bankruptcy, a process that is simply not capable of protecting the millions of Americans whose finances are intertwined with AIG's.

The Government rescue of AIG in the fall of 2008 was directly shaped by these realities. We had to protect the economy and the finances of millions of Americans. We could not have anticipated the magnitude of AIG's problems and we had no way of letting it fail without disastrous collateral consequences. We had to intervene, and I am thankful we did.

I do not mean to say that I am happy we needed to intervene. Taxpayer money should not have to be spent to save a misguided and mismanaged enterprise. But the fundamental problem lies not in how we intervened, but why we needed to intervene. We need to modernize our regulatory structure by creating a systemic risk regulator and resolution authority so any large firm that fails can be liquidated without destabilizing the system. Large financial institutions of this country will always play a role that is essential to our economic growth, but they must only be permitted to grow and interconnect throughout our economy under careful oversight and with a mechanism for allowing those connections to be broken safely.

Thank you, Mr. Chairman, and I would be happy to answer any questions.

[The prepared statement of Mr. Paulson follows:]

Embargoed until:
10:00 a.m.
January 27, 2010

Testimony by Henry M. Paulson
Before the House Committee on
Oversight and Government Reform
January 27, 2010, 10:00 a.m.

Chairman Towns, Ranking Member Issa, and distinguished Members of the Committee.

I appreciate the invitation to testify before the Committee.

I was Secretary of the Treasury in 2008. In that role, I had the privilege to work with the many talented men and women in government and the private sector who labored to pull our nation back from the brink of disaster.

The decision to rescue AIG was correct, and I strongly supported it. An AIG failure would have been devastating to the financial system and the economy.

Today's hearing relates to payments to AIG's credit default swap counterparties. I was not involved in any of the decisions made with respect to those payments, nor was I involved in any of the decisions about AIG's public disclosure of those payments. Those matters were handled by the Federal Reserve Bank of New York and the Federal Reserve Board. They sought to make appropriate decisions on those matters, and I am confident that this review will show that they did.

* * *

I have limited knowledge on the topic of immediate interest to the Committee, but I will share my observations.

The basic facts of the government's involvement with AIG are well known. I will recount them only in brief. On September 16, 2008, the Federal Reserve Board, with the full support of Treasury, announced that it was authorizing the Federal Reserve Bank of New York to lend up to $85 billion to AIG pursuant to its authority under the Federal Reserve Act. This loan was secured by AIG's ownership interest in its subsidiaries, and the U.S. government received a 79.9% equity interest in AIG. Simultaneously, the CEO of AIG was replaced. In early October, the New York Fed extended AIG another $37.8 billion in credit.

Unfortunately, these actions did not sufficiently abate the problems at AIG. The company faced mounting losses, and it faced potential ratings downgrades which would trigger tens of billions of dollars in collateral calls which, without an equity infusion, would have led to its failure—a failure that would have collapsed our financial system and devastated millions of Americans.

To address these problems, on November 10, 2009, Treasury and the Federal Reserve announced plans to restructure AIG's finances. Treasury announced that it would provide $40 billion from its TARP funds to stabilize AIG's capital structure, in return for

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senior preferred shares in AIG and stringent restrictions on golden parachutes and executive bonuses. At the same time, the Federal Reserve announced that it had authorized the New York Fed to set up two facilities which would handle certain AIG assets that were subject to the greatest risk of a devastating collateral call in the event of ratings downgrades.

The combined actions of Treasury and the Fed were effective. Despite AIG's breathtaking third-quarter losses, the company did not fail, and we avoided the disastrous consequences that would have accompanied such a failure. Although the road to complete recovery is slow and unemployment is still high, had AIG failed I believe we would have seen a complete collapse of our financial system, and unemployment easily could have risen to the 25% level reached in the Great Depression.

* * *

The rescue of AIG was necessary, and I believe that we in government who acted to rescue it—including Secretary Geithner, Chairman Bernanke, and me—acted properly and in the best interests of our country. The reasons the rescue of AIG was necessary are well worth examining. I believe they are representative of the causes of other aspects of the crisis and indicate where regulatory reform is necessary. There are three reasons we needed to intercede to save AIG that stand out in my mind.

<u>First</u>, AIG was incredibly large and interconnected. It had a $1 trillion dollar balance sheet; a massive derivatives business that connected it to hundreds of financial institutions, businesses, and governments; tens of millions of life insurance customers; and tens of billions of dollars of contracts guaranteeing the retirement savings of individuals. If AIG collapsed, it would have buckled our financial system and wrought economic havoc on the lives of millions of our citizens.

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<u>Third</u>, AIG could not be effectively wound down. Unlike failed depository institutions which can be taken over by the FDIC with little or no harm to depositors, or the GSEs which were seamlessly placed into conservatorship by Treasury and the Federal Housing Finance Agency, there was—and is—no resolution authority available to wind down a failing institution like AIG. The only option is bankruptcy, a process that is simply not capable of protecting the millions of Americans whose finances are intertwined with AIG's.

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Thank you, and I would be happy to answer any questions.

Chairman TOWNS. Thank you very much for your testimony.

Let me say that you were deeply and aggressively involved in dealing with the financial crisis. We saw that with AIG, of course, and Bank of America, and with the TARP. My question is why did you sit on the sideline and not use your considerable influence to call the CEOs of the counterparties to get them to take a haircut? Why wouldn't you do that? I mean, you are a person that was very influential in all of this, and I can't understand why you wouldn't do that.

Mr. PAULSON. Well, Mr. Chairman, as you indicated, I had no involvement at all in the payment to the counterparties, no involvement whatsoever. Now, to explain this, we worked very collaboratively during the crisis. There was a lot going on, coming at us from all sides, and whichever agency had the authorities took responsibility for execution. And this was clearly a case—it was a Federal Reserve loan. They had the authority to make it and administer it, and they had the technical expertise to do the restructuring.

Chairman TOWNS. But I just see it a little strange that you would sit on the sideline and not help the American people in terms of—I mean, you were so involved in the early stages and throughout the process——

Mr. PAULSON. Mr. Chairman——

Chairman TOWNS [continuing]. And then to sit on the sideline at a time like this, I just find that——

Mr. PAULSON. Mr. Chairman, anybody that knows me knows I was not sitting on the sideline. I was not involved in this issue, but I was involved in many other issues every single day of the week, including weekends. So I didn't spend——

Chairman TOWNS. Why not? Why wouldn't you be involved in this?

Mr. PAULSON. Because this was a Federal Reserve loan; they had the authority, they had the technical expertise. As I said in my testimony, I have great confidence in the professionalism, the integrity, the motives, the abilities of the people that were handling this. So this was their job to handle and I was working on many other things which were in my bailiwick.

Chairman TOWNS. Let me ask another question. Why wouldn't you let AIG go into bankruptcy? Why not?

Mr. PAULSON. If AIG had failed—this was a huge financial organization, interconnections throughout the economy. If it had failed, with the system as fragile as it was, I believe it would have taken down the whole——

Chairman TOWNS. Can you talk directly into the microphone? They are having problems hearing you.

Mr. PAULSON [continuing]. I believe it would have taken down the whole financial system and our economy. It would have been a disaster. Today, after all the actions that have been taken by the U.S. Government, we still have this terrible 10 percent unemployment level. I believe that if the system had come down and failed, we could easily have had unemployment reaching or exceeding the 25 percent level we had in the Great Depression; we would have lost many additional billions of dollars in American savings; home prices would be much lower than they are today.

So as unattractive as the Government rescue of AIG was—and none of us that supported that found that to be an attractive or desirable option—it was just much, much better than the alternative, which would have been economic disaster in this country.

Chairman TOWNS. I now yield 5 minutes to the gentleman from California, the ranking member.

Mr. ISSA. Mr. Chairman, I would ask that we go to the Members who did not have an opportunity in the first round. Mr. Chairman, I would also ask this one thing. Will you agree, since the Secretary said he would answer our questions, to join with me in ensuring that all questions are answered or that we bring the Secretary back, assuming he does not answer them for some reason?

Chairman TOWNS. So ordered.

Mr. ISSA. Thank you.

Mr. Luetkemeyer would be next of those waiting.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

Mr. Paulson, one of the things that we are looking into here with AIG, can you explain to me, AIG and their Financial Products, was that a subsidiary of AIG or was that part of their business model?

Mr. PAULSON. I believe it was part of the business model.

Mr. LUETKEMEYER. There wasn't a separate entity that was separately capitalized?

Mr. PAULSON. It was clearly at the holding company and it was part of——

Mr. LUETKEMEYER. The thing that makes——

Mr. PAULSON. It wasn't part of an insurance business model, but it was sure part of the company's business strategy.

Mr. LUETKEMEYER. Because it makes a big difference. If it is not part of the insurance product company and it is a subsidiary that is separately capitalized, you can let that thing go down and it doesn't impact the insurance part of it, which I believe it was. Is that not correct?

Mr. PAULSON. Well, I would say this to you. This company was so big and intertwined that it was—if there was any way that the people who were working on this could have found a way to just hive off and let one small part of the company go down——

Mr. KUCINICH [presiding]. Would the gentleman suspend? Mr. Paulson, excuse me. We want to make sure that Members can hear your testimony.

Mr. PAULSON. OK.

Mr. KUCINICH. You know, it is amazing with so much money in this Federal Government, we don't have a better sound system. But I am going to need you to speak as closely to that mic as you can so everyone can hear you.

Mr. PAULSON. OK.

Mr. KUCINICH. Thank you. You may continue.

Mr. PAULSON. So to just be clear, there was no way to hive off and handle this situation differently. There was a very few days to act to prevent bankruptcy with no wind-down powers to let this company be liquidated and avoid bankruptcy.

Mr. LUETKEMEYER. Well, with all due respect, if it is a separate entity, a subsidiary, it could go beyond and the rest of it could still stand on itself, sir, but that being——

Mr. PAULSON. Well——

Mr. LUETKEMEYER. Let me move on with another question very quickly. In Secretary Geithner's testimony, he indicated that he felt that, contractually, the contracts that we had, the investments that were made by foreign banks into AIG, that they were involved with, needed to be adhered to and worked with. Was the Government a part of those contracts?

Mr. PAULSON. As I have said in my testimony, I had no involvement with the payment of any of those contracts. I just was not involved in that matter.

Mr. LUETKEMEYER. So the Government wasn't a party to the contracts, then.

Mr. PAULSON. What?

Mr. LUETKEMEYER. The Government wasn't a party to the contracts.

Mr. PAULSON. Again, this was not something that I was directly involved in. I said that I very much trust the motives and the abilities and the judgments of the people that made those decisions, but I wasn't party to them and I can't answer that question.

Mr. LUETKEMEYER. OK. Well, that's one of the frustrations. I appreciate your candor, but my frustration with the Chair in that we don't get full testimony and be able to get all the questions asked and then answered so we can come to you with what we feel is good information to be able to get some good back and forth here. So I apologize to you.

Let me move on to something else. I know right now we are looking at, and the President has proposed, some too-big-to-fail sort of strategies to try and address the issue of too-big-to-fail. Where are you in this debate? What do you think about the proposal that is on the table right now, sir?

Mr. PAULSON. When I was Secretary of the Treasury, I put out a regulatory blueprint, and I still believe that is the way to go. I am very—I think it is essential that we have wind-down authorities, resolution authorities so that any financial organization, no matter how big, can be liquidated outside of the bankruptcy process without taking down the rest of the economy.

So I think that is essential, and there are some parts of the proposals that are up here being debated by Congress which are the same as in the regulatory blueprint we put forward, a big one being the systemic risk regulator, and I am strongly in favor of a systemic risk regulator.

Mr. LUETKEMEYER. Do you believe that we need to take the risk investments that are part of many of the big banks right now and take them off the books and have a subsidiary for this, so we can go back to Glass-Steagall firewall there?

Mr. PAULSON. That is not my recommendation. I believe that when you look at the crisis, what I saw in the crisis was that it was across a number of types of financial institutions, and the excessive risk-taking I saw was not limited to one business activity, it was much broader than that, and I think we need a broader approach. So, again, what I favor is a systemic risk regulator and wind-down authorities is the way I would handle that.

Mr. LUETKEMEYER. Well, one of the problems I have with what you are suggesting, sir, is that suddenly now we have the taxpayers, through FDIC insurance, on the hook for these risk takers who are out here. I think it is important that we take these things off the books and have a subsidiary. If it goes down, it goes down and the banks and the insurance funds and the taxpayers as a whole are not on the hook for all this. I think it is very important we go down that road, because I think what you have done with AIG is suddenly used the Federal Government as the official underwriter of all investments in the world. If we are underwriting foreign contracts, investments, what have we done? We have gone down that road.

I appreciate your comments and I yield back to the Chair.

Mr. KUCINICH. The gentleman's time has expired.

The Chair, in keeping with the necessity of making sure that Members who did not ask questions the last round, are given a chance to go first. We recognize Mr. Tierney. Thank you for your patience and you may proceed for 5 minutes.

Mr. TIERNEY. Thank you, Mr. Chairman.

Mr. Paulson, thank you for being here this morning. So you were in full agreement with not allowing AIG to go bankrupt.

Mr. PAULSON. Absolutely.

Mr. TIERNEY. I think, back home, people don't know where to give the credit for this, so I want to make sure we give credit where credit is due if that was a good decision. People see Mr. Geithner now as Treasurer, and they think the decisions were all made by him when he was Treasurer. In fact, these were decisions made in 2008. You were President Bush's Secretary of the Treasury, correct?

Mr. PAULSON. Absolutely.

Mr. TIERNEY. And Mr. Bernanke was the head of the Fed. Then, of course, we had the New York Federal Reserve Board participating in these conversations as well. So you were pretty much the group that decided that they should give $85 billion in September to AIG. Those were mostly the participants, am I right?

Mr. PAULSON. Yes. As I said in my testimony, I very much supported that rescue.

Mr. TIERNEY. And then in November it was the same group—you, as President Bush's Secretary of the Treasury, Mr. Bernanke, and the New York Fed—decided to give additional funds to AIG, some of which we used to pay the counterparties to the contracts, right?

Mr. PAULSON. Yes. In November, in the TARP, we made a $40 billion capital investment, and then the Fed put some additional money in, which was used up for the contracts.

Mr. TIERNEY. Just so we are clear—we are giving credit here—the TARP, the $700 billion in TARP, in fact, was during your term as Secretary of the Treasury under President Bush.

Mr. PAULSON. Yes. I am proud of that. So that——

Mr. TIERNEY. That was your idea, was it, the TARP?

Mr. PAULSON. It was a number of our ideas, but, yes, and that is something I am proud of and something that was very necessary.

Mr. TIERNEY. And the $85 billion that was loaned to AIG was not appropriated by Congress; nobody asked Congress to make a vote on that, am I right?

Mr. PAULSON. No, that was a decision taken by the Fed with the support of——

Mr. TIERNEY. What source of money did they use to get that $85 billion?

Mr. PAULSON. They used their funds.

Mr. TIERNEY. And their funds emanate from where?

Mr. PAULSON. From the U.S. Government.

Mr. TIERNEY. Well, were they fees from other banks, did they come from your Treasury? Where did they come?

Mr. PAULSON. They come from—the Fed, obviously, can print money.

Mr. TIERNEY. OK. And did they take money that they had from fees charged to member banks or did they print money to accommodate this $85 billion?

Mr. PAULSON. You would have to ask the Fed that.

Mr. TIERNEY. You are not aware through any discussions where that was?

Mr. PAULSON. I would like them to answer that question.

Mr. TIERNEY. Well, you may not like to answer the question, sir, but if you know the information, I am asking you to share with us what is your best understanding of where that money came from.

Mr. PAULSON. My best understanding is all dollars are green, so those are ultimately taxpayer dollars, and that was why——

Mr. TIERNEY. We are painfully aware that they are taxpayer dollars, sir.

Mr. PAULSON. That was why the Treasury was supportive and we were very supportive of that transaction.

Mr. TIERNEY. OK, we all understand that the full faith promise comes from the Government on that and they were taxpayer dollars, we are painfully aware, but I am asking you whether, since they didn't come to Congress for an appropriation, whether the $85 billion came from fees charged to member banks, was newly printed money, or some combination of the both.

Mr. PAULSON. I don't believe it came from fees charged from member banks.

Mr. TIERNEY. All right, thank you. Now, we got to the point where a decision had to be made about whether or not to let AIG go bankrupt. Later it came to a point whether or not to pay the counterparties 100 percent on those contracts or not. But once the decision was made not to let them go bankrupt, you lost any leverage, really, to argue in terms of getting—being able to pay less than 100 percent. Is that a fair statement?

Mr. PAULSON. As I said, I didn't participate in those decisions regarding payment, and I also said we didn't have the wind-down powers.

Mr. TIERNEY. But you were involved—I forget how many Congresswoman Kaptur said that there were phone calls between the New York Fed and you.

I will yield.

Ms. KAPTUR. 225.

Mr. TIERNEY. 225 telephone conversations between the head of the New York Fed and you during this period of time, so I think we might be fair in assuming that you were discussing some of these matters?

Mr. PAULSON. Well, we had many matters to discuss——

Mr. TIERNEY. And this was one of them, right?

Mr. PAULSON [continuing]. Over a range of things, and the matters we discussed—we clearly discussed the rescue. As I said, I did not have involvement and was not discussing——

Mr. TIERNEY. Here is my final question. I need your help with this. Most people at home hear people draw the conclusion that not to allow AIG to go into bankruptcy would have been devastating because the consequences would have been severe. It would be enormously helpful if you could put yourself in the position of the local bookkeeper for a medical firm or housekeeper or lawyer or teacher's aide. How specifically would that individual have been harmed if you had not made the decision to not allow AIG to go bankrupt? What would have been the consequence to them?

Mr. PAULSON. And that is the right question, Congressman, because they were the real victims. They would have lost jobs, would have lost——

Mr. TIERNEY. But how? How would that have happened? Show me, from the time you made the decision, what would it have spiraled down to affect their lives.

Mr. PAULSON. Well——

Mr. KUCINICH. The gentleman's time has expired, but the witness would be pleased to answer his question, I hope.

Mr. PAULSON. OK. What I believe, we were—at around the time of the AIG rescue, when markets were frozen, we had a situation in this country where even blue chip industrial companies were having trouble financing. I knew we were on the brink. That if AIG had gone down, I believe that we would have had a situation where Main Street companies, industrial companies of all size would not have been able to raise money for their basic funding, and they wouldn't have been able to pay their employees, they would have had to let them go. Employees wouldn't have paid their bills. This would have rippled through the economy.

Today, Congressman, we have, after everything that was done, all the resources, we have 10 percent unemployment. I believe we easily would have had 25 percent unemployment. Today we have home prices that have dropped precipitously in some parts of the country. Home prices would have gone much lower. AIG guaranteed tens of billions of dollars of savings for retirement savings for Americans. There would have been great losses. This would have been an economic nightmare.

Mr. KUCINICH. Thank you, Mr. Paulson.

Mr. TIERNEY. Thank you.

Mr. KUCINICH. The Chair recognizes Mr. Souder.

Mr. SOUDER. Thank you. I have a variation of the same question you were just going through, because one of the problems we have is that it appears that AIG was treated differently than other companies throughout this whole thing in this sense, that the holders of the debt were paid at par, which means that, in effect, the banks got 100 percent but, for example, GM creditors, small businesses all across America, and other companies that were let go, they got 10 cents on the dollar or 30 cents on the dollar; and it is part of a fact, a perception that was unfair, that Wall Street was covered but Main Street wasn't, in debt.

Now, AIG was different in what sense? Now, I know—was it 120 separate finance companies and 80 insurance, or is that flipped?

Something like that. In other words, it was a collection, it wasn't one.

Mr. PAULSON. It was a big complex collection of companies, correct.

Mr. SOUDER. And that if the insurance divisions were separated and came under State, part of the argument is State regulation, that they were so intertwined with the finance.

But let me ask one other question before we get into details of that. You said bankruptcy wasn't an option, but it also meant that did you try to put pressure on the people who held the debt to write down some of their debt, or once you made the statement "we weren't going to let it fail," were they just playing hardball in saying we weren't going to write down anything? Why didn't they get the same pressure that GM suppliers had and everybody else to write down their debt?

Mr. PAULSON. As I have said—and this isn't me trying to suggest anything was done wrong—I had nothing to do with that, so I was not involved in the negotiation. I was not involved in anything surrounding those payments. But I will explain one thing to you which is fundamental for you to understand is the Government—we have an antiquated regulatory system and a lack of the necessary authorities. So if there was a bank, there is a way to wind that down. But this was a non-bank and there was——

Mr. SOUDER. OK, I understand that. Let me——

Mr. PAULSON. There is no way to avoid it.

Mr. SOUDER. Let me ask you—there is no way except the threat of real bankruptcy. If you are a bank and think you can negotiate at par and get a full percent, and you don't have a threat of bankruptcy, the question is did anybody threaten them?

Did anybody say that we are not going to—I mean, did we, in effect, yield the debate at the beginning, they played hardball, and we had no way to do it; that if in effect you would have even threatened to say, hey, we can cover the insurance people, but the finance side over here, you better negotiate down or that side will go bankrupt, and then you would wind up probably having to do what we did in TARP anyway, which was put cash reserves into the banking system to try to cover the fact that the bankruptcy went out.

Would that not be true? In other words, had they gone bankrupt and there really was a catastrophic threat—which I believe, because I voted for TARP—a catastrophic threat, wouldn't you have just had to put more money in the banking system, but not necessarily at par?

Mr. PAULSON. As I said, Congressman, I wasn't involved in that, so I can't——

Mr. SOUDER. You are saying the New York Fed did that.

Mr. PAULSON. I can't comment beyond what I have said.

Mr. SOUDER. When you got involved, once TARP was there, the decision was already made that it wasn't going to go bankrupt, is that correct?

Mr. PAULSON. When I—first of all, I was involved in supporting the initial rescue, and then——

Mr. SOUDER. So you were involved. Just a second. You were involved?

Mr. PAULSON. Yes.

Mr. SOUDER. And did you advise the Fed to try to get what they could and not to pay at par?

Mr. PAULSON. What the Fed—the initial rescue was not the—was not when they dealt with the payment to counterparties. So I supported the Fed on the initial loan, and then, later, in November, the situation had deteriorated to the point and values in insurance businesses all around the world had deteriorated to the point that this was a company that would go down without capital. So now we had capital and my team and I participated in making that decision, made the decision to put $40 billion of equity into AIG.

Mr. SOUDER. The problem that I have is that it appears to me that AIG was treated differently, so much so. Even listening to that, it is like, "well, we put some money in initially and then we put more money in because they couldn't fail;" where, in the other—everything from Citibank to Merrill Lynch to everything else there were processes where there were conditions on money coming in, where there were guidelines on money coming in and they used the leverage of the threat of bankruptcy to do that. Then, in this case, it appears that it was different, and it partly is that the creditors were different.

Furthermore, some of the critical information here was withheld from being public at the request of the New York Fed. Had that been public, people would have seen it. And there was an attempt to even keep it quiet because that was critical, that information, to understand what was going on behind. And it is extremely frustrating to all of us on this committee—you can hear it in different types of questions—about how this came to be, and I don't think there has been a compelling case made that AIG is unique.

Mr. KUCINICH. The gentleman's time has expired, but I would say that if Mr. Paulson wants to respond to the gentleman, you may do so, and, if not, we will go to the next questioner.

Mr. PAULSON. I have no response.

Mr. KUCINICH. OK. I thank the gentleman.

The Chair recognizes Mr. Kanjorski.

Mr. KANJORSKI. Thank you very much, Mr. Chairman.

Welcome back, Mr. Paulson. You really miss Washington, I assume.

Mr. PAULSON. You can't guess how much.

Mr. KANJORSKI. I listened to the comments of the Secretary, your successor, and now you, and I am listening to the Members' questions and how much memory is lost in a year or 14 months from those fateful days in September and October, which all of us hope we never relive, but, in fact, were very much significantly different than today, and the coolness of being able to answer.

One of the questions I was particularly interested in, because I was very involved at that time with AIG and what was happening from my aspect of having some jurisdiction over insurance, is that as I understand it, because of Financial Products in London was without assets and had a tremendous involvement in counterparty positions for about $2.8 trillion, and whose counterparty positions were starting to fail and they had to honor them, their initial internal decision of AIG was to use the assets of the world's largest insurance company, and they sought permission and it was pending and finally approved by their regulator, the State of New York, to take assets out of the insurance companies, about $30 billion, and use those assets to cover their exposed counterparty and positions.

Now, if that had happened at that time, those insurance companies would have failed because their assets would have been taken, converted, and there wouldn't have been enough to cover the counterparties, so it would have wiped out the insurance companies, which in turn would have affected every insurance holder in the country that was involved with AIG at the time, and would have been a catastrophic collapse of the insurance industry, notwithstanding the counterparty derivative position.

Now, luckily, the regulator in the State of New York didn't grant us permission to use that $30 million until much later, when it was futile. At that point, the losses on the counterparty positions, I think, rose to $55 billion and were climbing on a daily basis, and that is when the infusion of funds that you talk about, adding equity to AIG or the capacity through the use of Government funds to cover those counterparty losses. They didn't cover all those losses and, subsequently, within probably 30 days, another huge amount of money was infused into AIG's various corporate structures to get some stability.

And not that I could say nothing has changed from that, but that was the significant circumstances in this month or 2 months after September 18th that everybody was faced with. But, as I understand it, the Federal Reserve was the person with the checkbook under the incidence under 3.13 powers, they were just plugging that money in.

And it wasn't a decision made at the Secretary's level of Treasury or at the Presidential level, it was a Federal Reserve regulator level that was making that decision; and I dare say regulator not for AIG, but regulator that had regulation over some of the largest banking institutions in the world, that if their counterparty positions weren't honored, they would have immediately collapsed. And that is what we were calling the meltdown. Everything was going to implode and you had to stop it at the headwaters, not wait until it got out to the little dams out in the stream.

Is that relatively the correct position?

Mr. PAULSON. I would say, without signing off on every fact you mentioned, I would say you've got it in the sense that this was a very complex company and there was—if it had gone into bankruptcy, it would have been a huge mess and it would have—one part of the company would have contaminated the other and it would have rippled through the U.S. economy, and the result would have been absolute disaster.

Mr. KANJORSKI. Mr. Chairman, I know there are other questioners. I have had the opportunity to ask some today, so I yield back the balance of my time.

Mr. KUCINICH. I thank the gentleman for his courtesy.

Before I recognize Mr. Bachus, I want to take the liberty, as Chair, to recognize students from Padua Franciscan High School in Parma, OH, visiting the Capitol and seeing their government at work right here. So welcome, you and your teacher and we are pleased that you stopped by for a visit. Thank you.

The Chair recognizes Mr. Bachus of Alabama.

Mr. BACHUS. Welcome, former Secretary. Secretary Paulson, March 2009, March 16th was when AIG was—the payments were made to AIG or guaranteed. Leading up to that, you participated in several meetings about AIG, is that correct?

Mr. PAULSON. Prior to March of——

Mr. BACHUS. Of 2009.

Mr. PAULSON. Prior to March? Yes, I had a number of meetings about AIG as we were putting in capital.

Mr. BACHUS. I know one of the meetings—I am looking at March 24th, my questioning of Mr. Geithner, he mentions, Secretary Geithner, that you—he said that he and you met with AIG to discuss Lehman's failure.

Mr. PAULSON. To discuss what?

Mr. BACHUS. September 14th. Now, that was 2 days before.

Mr. PAULSON. Oh, yes. You are saying—you were talking about March 2009. I think you are talking about September 14, 2008.

Mr. BACHUS. That is right. OK. I stand corrected. That discussion—but you participated in some of the discussions about AIG and their financial condition leading up to——

Mr. PAULSON. Yes. And that weekend of September 13th and 14th was the weekend when we had financial institutions together working to come up with a solution to prevent the failure of Lehman, and it was that weekend that we learned also about AIG, and I had two meetings over the course of that weekend at the New York Fed with Tim Geithner, with officials from AIG.

Mr. BACHUS. In those meetings, was there any discussion of asking the counterparties to take less than 100 percent?

Mr. PAULSON. Was there any discussion of what?

Mr. BACHUS. Any discussion of the counterparties taking less than 100 percent?

Mr. PAULSON. I certainly don't recall any. We were talking about the financial problems that AIG had and it was clearly—they clearly had issues with counterparties.

Mr. BACHUS. What?

Mr. PAULSON. They clearly had issues with counterparties, because that was the crux of the issue, a potential ratings downgrade which would cause the company to have to post collateral. So that would lead to——

Mr. BACHUS. So the obligation to the counterparties was discussed?

Mr. PAULSON. Well, obviously, that was the issue. Any institution that is facing failure is going to have an issue with paying creditors.

Mr. BACHUS. You know, once that intervention occurred, then really the taxpayers, the U.S. Government owned 79.8 percent of AIG, more or less. Is that correct?

Mr. PAULSON. Yes.

Mr. BACHUS. That being the case, I see in this same, March 15, 2009, this is skipping forward to March 2009. Secretary Geithner emailed William Dudley and Edward Quince and he said, "Where are you on the AIG counterparty disclosure issue? Are you for disclosing or not?"

Mr. ISSA. Would the gentleman yield? Could you put up slide 1 so they could see it? Thank you.

Mr. BACHUS. What would your advice have been on whether or not that should have been a public disclosure of the counterparties and their obligations? And would the fact that really the taxpayers own over 79 percent, almost 80 percent of the company have made any difference?

Mr. PAULSON. Well, as a general proposition, I am very much for disclosure, but I wasn't part of this. I had nothing to do with that decision. And I am not going to sit here now and second guess others that were, you know, that I know people with strong integrity and good will tried to do the right thing.

Mr. BACHUS. Well, just take a situation where you do have a company that is, you know, 80 percent-owned by the U.S. Government. Would that tend to make you think that there ought to be disclosure of their obligations?

Mr. PAULSON. Well, public companies——

Mr. KUCINICH. The gentleman's time has expired, but you can answer his question.

Mr. PAULSON. I will be brief. Public companies have disclosure obligations and that is governed by the SEC, and I think those need to be adhered to.

Mr. BACHUS. Thank you.

Mr. KUCINICH. OK, I thank the gentleman.

The Chair recognizes Mr. Cummings of Maryland. You may proceed.

Mr. CUMMINGS. Mr. Paulson, good seeing you again. Let me ask you this. Mr. Paulson, do you realize that a lot of the American people believe that there is a sort of Wall Street club, and that, let me finish, that you all play golf together and you have a lot of fun, and then you, you know, when the billions come around you are able to kind of distribute them.

I mean, I am just saying, do you know that is how people feel?

Mr. PAULSON. I sure do. And even though——

Mr. CUMMINGS. Can you keep your voice up?

Mr. PAULSON. I said even though I am not a golfer, I sure know that is how people feel.

Mr. CUMMINGS. Yes, and when they see these deals going on, then the next thing they do is they begin to look at where people work, and then they see the relationships and then they say, well, you know, we don't have a chance because it seems like they are kind of looking out for themselves, but not looking out for us.

So, you know, you just gave a statement about transparency, and, you know, and I think one of the things that bothers people was when they don't see transparency, then they begin not to trust. And when they begin not to trust, it becomes very difficult for them to go along with any program.

And then when you put on top of that they can't see themselves benefiting, and I know that you mentioned that if we didn't do what we did, unemployment may have gone up to 25 percent, but it is hard for people to even see that.

You understand?

Mr. PAULSON. Yes, I, Congressman, you have it. And that is, people are very, very angry, and I understand it, why they are angry, and they are rightfully so, because they don't see the connection.

And they don't recognize that what was done wasn't done for the bank. They were going to be the victims if we didn't step in.

Mr. CUMMINGS. And so among the conditions in the TARP-AIG-SSFI Investment Senior Preferred Stock and Warrant summary of senior preferred terms, as posted on the Treasury Department's Web site, the following condition was noted: "The annual bonus pools payable to senior partners in respect of each of 2008 and 2009 shall not exceed the average of the annual bonus pools paid to senior partners for 2006 and 2007."

Do you believe it was appropriate for Treasury to allow AIG to create any bonus pool for senior partners, considering it had just found it necessary to extend $40 billion to the firm through the TARP?

Mr. PAULSON. I am not going to get into second guessing decisions that were made at Treasury about bonuses. I realize this was a very difficult decision because the taxpayer had a lot of money in this company.

Mr. CUMMINGS. Right.

Mr. PAULSON. And this company needed to perform well and needed to hold the team together in order to repay taxpayers.

Mr. CUMMINGS. Right, and the taxpayers were saying to themselves, look, these are our tax dollars. We work hard for these tax dollars and now these guys, who screwed up everything, are getting bonuses.

Mr. PAULSON. Yes, you are right. No one, me included, likes to see private business profit from taxpayer assistance. That makes people angry. And to me, I just hope that part of that anger is not a diversion from what we need to do, but is an incentive to fix the system so that we will have resolution powers and never again will have a company that is so big, too big to fail, so the taxpayer has to come and put money in; that a company can be liquidated and wound down in a way in which the taxpayer is not on the hook again.

But so I understand there is that anger out there and that frustration. I think it is very understandable. And I think there are a number of ways to do something about it, but the best way to do something about it is reform the system so that we don't ever again have to bail out a big institution, rescue a big institution. It could be liquidated if it fails.

Mr. CUMMINGS. Now, with regard to the original Treasury TARP investment in AIG, was this structured as a loan or as an equity investment?

Mr. PAULSON. Congressman, it was an equity investment.

Mr. CUMMINGS. And was this in the AIG parent holding company or in the individual subsidiaries?

Mr. PAULSON. This was in the parent. This was a $40 billion equity investment because the company needed equity.

Mr. CUMMINGS. And was it made subordinate to any other creditors of AIG?

Mr. PAULSON. Well, a preferred is by definition senior to the common, and subordinated to the other creditors.

Mr. CUMMINGS. And how does this compare to the various Federal Reserve investments in AIG?

Mr. PAULSON. Well, this is subordinate to the other Federal Reserve investments in AIG because a determination was made. The rating agencies had basically said that you need to put capital in this institution or there will be a downgrade, and then they would have precipitated the failure.

Mr. CUMMINGS. And why was it structured in this way?

Mr. PAULSON. It was structured in that way because that is the way a preferred needs to be structured. It wouldn't have been capital if it hadn't been subordinated to the other liabilities.

Mr. CUMMINGS. I see my time is up.

Thank you, Mr. Chairman.

Mr. KUCINICH. I thank the gentleman.

The Chair recognizes Mr. Stearns from Florida. You may proceed for 5 minutes.

Mr. STEARNS. Thank you, Mr. Chairman.

Mr. Paulson, Mr. Geithner has testified that he recused himself during this counterparty negotiation. Did you know that while you were Secretary of Treasury?

Mr. PAULSON. I knew that——

Mr. STEARNS. Just yes or no.

Mr. PAULSON. Yes.

Mr. STEARNS. You did know. OK.

Mr. PAULSON. Tim Geithner did not participate in any—I didn't view him as a decisionmaker. I viewed him as recused.

Mr. STEARNS. OK. Did he call you up and advise you that, I have recused myself? Did he call you up?

Mr. PAULSON. He——

Mr. STEARNS. How did he notify you?

Mr. PAULSON. Well, he told me on the phone that he did not think it would be appropriate for him to be viewed as a decisionmaker.

Mr. STEARNS. Did you know he never got a letter? All he did, he testified that he recused himself. He decided. He put up a flag and said, I recuse myself; I am not going to be involved with the counterparty negotiation. He didn't get a—like you went to the White House Counsel and you went to Secretary of Treasury, you got a letter. He never got a letter. He never got a written confirmation of his recusal.

Did you know that? Do you know that he was just doing it on his own by his own volition?

Mr. PAULSON. I did not know the details.

Mr. STEARNS. OK. Did you think a person who would recuse himself in this crisis we had, that he could go about and operate in his present job and not have a conflict of interest? Did it ever occur to you to say, "gee, the chairman of the Federal Reserve is in this crisis; we are having the counterparty negotiations, and by golly, he is going to step aside and says he knows nothing about it." That is what he is saying today. Doesn't that seem sort of fakey to you?

Mr. PAULSON. No, it didn't, because I thought it was an extraordinary position we had to have a presently New York——

Mr. STEARNS. OK, I understand. Now, the next question in open testimony that his chief of staff, while he was chairman of the Federal Reserve, was a former employee of Goldman Sachs. Did you know that?

Mr. PAULSON. Yes.

Mr. STEARNS. Did you ever call his chief of staff, former employee of Goldman Sachs, during the process for the counterparty negotiations? Did you ever call him? If I go through the logs, will I see your name calling him?

Mr. PAULSON. His chief of staff, who is a former employee of Goldman Sachs——

Mr. STEARNS. And he worked for you when you were CEO.

Mr. PAULSON. He didn't take on that job until after I had left, and he had become Treasury Secretary.

Mr. STEARNS. Did you ever call him at all? If I go back to the logs, will I find that you called Geithner's chief of staff, former employee of Goldman Sachs, during the counterparty negotiations?

Mr. PAULSON. Yes, I, no, I didn't.

Mr. STEARNS. You never called him?

Mr. PAULSON. As I said, the former—his chief of staff, I think is the person you are referring to——

Mr. STEARNS. We didn't know about it until today.

Mr. PAULSON [continuing]. Is someone who became his chief of staff when he became Treasury Secretary after I had left office.

Mr. STEARNS. No, he said that while he was at the Federal Reserve, he was his chief of staff. That is what he said today.

Mr. PAULSON. I don't believe that was the case.

Mr. STEARNS. OK. All right.

Mr. PAULSON. But in any event, when he was——

Mr. STEARNS. OK, let me just go on. I have the time.

Mr. PAULSON. I talked with Tim.

Mr. STEARNS. Here is the problem I think a lot of us are having. Mr. Geithner said he was not involved with the counterparty negotiations. You are saying you were not involved. Oh, yes, you heard a little bit about it, but on November 6th when they gave $62 billion to all these parties who came in and looted AIG, all you guys say, I knew nothing about it. And yet it appears that this happened.

Now, recently Michael McRaith, who is director of the National Association of Insurance Commissioners, told the Senate Banking Committee, he said, you know, if AIG had gone in bankruptcy, we would have taken care of it. It would have been an orderly disposition. This is what he said: "AIG's insurance operations and their other companies would have simply—we would have simply bought up AIG's insurance assets, allowing a seamless delivery of AIG's insurance obligations."

So the question is, considering that the State Insurance Commissions would likely have seized AIG's insurance subsidiaries, protected policyholders in an AIG bankruptcy, why was it necessary to bail out AIG with taxpayers' money, based upon the testimony of the director of the National Association of Insurance Commissioners?

Mr. PAULSON. I respectfully disagree with him, and I believe that it is——

Mr. STEARNS. So you disagree with this guy, with all his knowledge, his years of experience?

Mr. PAULSON. I will just say many people with years of experience had some regulatory responsibilities with regard to AIG, but this company was had a huge problem, and it is case No. 1 on what is wrong with our regulatory system. There was no single regulator that had a line of sight on the total company. So there were regulators that looked at different pieces of it, and if the company had gone down, it would have been a huge mess.

Mr. STEARNS. Is your testimony—Mr. Geithner sort of implied. He scares Members of Congress. He scares the public. We are all scared. He said, "If AIG was not bailed out, this country would have collapsed." He intimated our Constitution would not have been able to be enforced. There would be a revolution in this country.

Do you think it is at that extreme if we let AIG go bankrupt, we would have had that kind of collapse and revolutionary spirit in this country? Is that what your position is today?

Mr. PAULSON. I certainly have never said that, but what I——

Mr. STEARNS. He implied that.

Mr. PAULSON. What I have said is I believe we would have had absolute economic disaster.

Chairman TOWNS. The gentleman's time is expired.

I will now recognize the gentleman from Ohio, Mr. Kucinich.

Mr. KUCINICH. Thank you, Mr. Chairman.

Secretary Paulson, thank you for being here today.

In your testimony, you state that in your capacity as U.S. Treasury Secretary, you were not involved in any decisions with respect to payments to AIG's counterparties and that you were not involved in any of the decisions concerning AIG's disclosure of those payments.

I would like to accept that at face value, Mr. Paulson, except the critical decisions concerning payments to counterparties were made after the passage of the Emergency Economic Recovery Act by Congress at your request, and the Emergency Economic Recovery Act made the Treasury Secretary responsible for the use of funds authorized by Congress. Negotiations on the counterparty payments by the Federal Reserve Bank of New York did not begin until November 6, 2008, and the funding of the payment of the counterclaims was backed by funds made available under the Emergency Economic Recovery Act.

So Mr. Paulson, doesn't it make it your responsibility to know how those funds were used?

Mr. PAULSON. I think you will find, Congressman, and I think SIGTARP reported this, that the TARP investment, the $40 billion TARP investment, was equity, and that those funds did not go into this Maiden Lane vehicle where the Fed loan——

Mr. KUCINICH. So you didn't have any knowledge of the counterparty payment transactions?

Mr. PAULSON. I did not.

Mr. KUCINICH. Are you telling us that?

Mr. PAULSON. I did not.

Mr. KUCINICH. And are you telling us that you were not aware of any of the discussions leading to the counterparty payments with any of the principals?

Mr. PAULSON. That is what I am telling you.

Mr. KUCINICH. And you are telling us that as Treasury Secretary, you had no role whatsoever in the decision on counterparty payments, that you didn't ask anyone any questions, that you never expressed an opinion on the matter, and you were completely unaware of the nature of proposed transactions until it was consummated, and no one asked you any questions about how these Emergency Economic Stabilization Act or the Recovery Act funds would be used to stabilize AIG, the one financial institution more than any other that was behind the crisis. You just didn't know.

Mr. PAULSON. Well, Congressman, we asked a lot of questions about the $40 billion TARP equity investment. That was something that was our job and it was our authority.

Mr. KUCINICH. Did you ask about the counterparty payments?

Mr. PAULSON. And as I said, the loan, that was a Fed authority and they had the authority and the technical expertise to handle that. And that was their job, and we were consumed with other matters and had great confidence in them to carry out their responsibilities very professionally and well.

Mr. KUCINICH. Well, you know, Mr. Paulson, no one disputes that you worked very hard throughout the crisis. It is well known you were personally talking with senior executives at all major financial institutions on your now legendary cell phone, which I might add is in the Museum of American History.

But how is it that you played no role in the handling of this AIG relief? That you didn't have an interest in it? How is it that despite Goldman Sachs' extensive role as a counterparty to an agent for AIG in transaction, your extensive personal network of associations within Goldman, which extended to several Goldman alumni on staff at Treasury, that you can say that you didn't have any knowledge, and by implication, no influence over the transaction? I don't understand that.

Mr. PAULSON. Well, it can't be any clearer. I assumed that Goldman Sachs—knew that Goldman Sachs and I assumed most other major financial institutions were counterparties, but I had no knowledge of what the individual claims were and my concern here was not about counterparty claims when we rescued AIG. My concern was about what was going to happen to the American economy and the American people.

And again, you need to understand when we worked together, Fed and Treasury, we had different authorities, different responsibilities, and there was so much going on that we had a lot to do, and they had the authority and responsibility for dealing with the loan——

Mr. KUCINICH. The thing that I have trouble with, though, is that the government gave Goldman Sachs, your former firm, a better deal than it had a right to expect. You heard the previous testimony here. It is mystifying how you, as Treasury Secretary, this could happen and you not really know anything about it unless you recused yourself from any discussions about AIG, or about Goldman Sachs.

Mr. PAULSON. I didn't have to recuse myself because the fact was no one discussed it with me, consulted with me. I was involved in other matters. This was a Federal Reserve authority and they had the technical expertise and that was their job.

Mr. KUCINICH. Thank you, Mr. Paulson. Thank you.

Chairman TOWNS. The time of the gentleman has expired.

Just so you know, we have four votes. At this time, I would ask if anyone has not [remarks off mic].

No, I am saying we have votes on the floor, and of course we have four votes and that we, due to previous agreement with Mr. Paulson, we are now going to allow him to go.

Mr. ISSA. Mr. Chairman.

Chairman TOWNS. Yes?

Mr. ISSA. Could we ask if Mr. Paulson could stay just for 5 more minutes to complete on our side? Two people will split time.

Chairman TOWNS. Two? Well, let me put it this way, then. Who all has not had an opportunity? One, two, three.

Mr. Paulson, could you give us another 7 minutes, and let me split 3½ and 3½?

Mr. PAULSON. Yes. OK. We can work it.

Ms. WATSON. Mr. Chairman, I would be willing to put mine in writing to Secretary Paulson if he would be willing to respond within a certain given time.

Chairman TOWNS. Mr. Secretary? Yes.

Mr. Secretary, there is a request in terms of if we give the questions to you in writing, you will respond.

Mr. PAULSON. Yes, we will get back to you.

Chairman TOWNS. Thank you very much. OK, yes.

Mr. BURTON. Mr. Paulson, you were——

Chairman TOWNS. Let's see how we are going to break this down first.

Mr. BURTON. You were one of the chief operating officers in Goldman.

Chairman TOWNS. Will the gentleman yield?

You are going to give us an additional 7, 8 minutes?

Mr. PAULSON. Is it? OK.

Chairman TOWNS. OK. Good. All right, so we will break it down four. OK.

Mr. PAULSON. It really will be 8 minutes, right?

Chairman TOWNS. Right; 8 minutes.

Mr. BURTON. You were one of the top officers for Goldman Sachs, right?

Mr. PAULSON. Yes, the top officer.

Mr. BURTON. And some of the people that work for Goldman Sachs went to work for Mr. Geithner?

Mr. PAULSON. I believe I know——

Mr. BURTON. Yes. And when you left Goldman Sachs and went to the Treasury, you were there 3 years and you got $200 million in tax benefits because you didn't have to pay capital gains on $500 million worth of stock. Right?

Mr. PAULSON. I would strongly disagree with that because——

Mr. BURTON. Well, that is what has been reported.

Mr. PAULSON. Let me just——

Mr. BURTON. Well, it is OK. You can respond. I will send a question to you in writing.

Mr. PAULSON. OK.

Mr. BURTON. The concern I have is the same concern Mr. Stearns has. You came before our Caucus very nervous, saying, oh, my gosh, the sky is falling. We have to come up with this money very, very quickly. You actually were visibly nervous when you came before our Caucus. And then we have this bailout of AIG, and you don't know anything about it. Mr. Geithner had nothing to do with it.

It just really boggles the mind that some of the biggest people involved in this whole thing from beginning to end had nothing to do with it. They didn't know. It makes you want to think that some clerk someplace was making these decisions. I don't think anybody is going to buy that.

You and Mr. Geithner and others were directly involved in making this decision, were you not?

Mr. PAULSON. Of course we were directly involved, and I said it in my testimony. I heard Mr. Geithner's testimony. I heard him say the same thing. I was very supportive of that decision to prevent the failure of AIG.

Chairman TOWNS. The gentleman's time has expired. I yield to the gentleman—who is next on my side? Mr. Lynch.

Mr. LYNCH. Thank you, Mr. Chairman.

Chairman TOWNS. Two minutes.

Mr. LYNCH. Right.

Mr. Secretary, I need to make this happen in 2 minutes. You were centrally involved with the negotiations regarding Bear Stearns when you insisted on a very, very low price on the part of the Bear Stearns shareholders in order to protect the taxpayer. It has been reported that you were very supportive of a $2 a share price in order to protect the taxpayers' interest.

And yet in this situation with AIG, and you were the CEO of Goldman Sachs back in 2006. There was a longstanding relationship there between AIG and Goldman Sachs that you were well aware of. Goldman Sachs was a major counterparty on a lot of these credit default swaps with AIG when you were the CEO at Goldman, and that relationship continued after you left.

You would have known that these people were—that Goldman was exposed here with these credit default swaps when the money went from the taxpayer to AIG and through to your former company.

And I guess the question that everybody has here is why, when you insisted on Bear Stearns taking a big haircut, why did you allow Goldman to be reimbursed, your former company, at 100 cents on a dollar in that situation? Why did you not weigh in on behalf of the taxpayer?

Mr. PAULSON. As I have said on a number of occasions, I did not know. I had no knowledge of the size of the claim of any bank and I had no involvement in a decision to make payments to the counterparties. None whatsoever. I was very supportive of the rescue of AIG because a failure of that company would have been disastrous.

Mr. LYNCH. Especially to Goldman Sachs.

Chairman TOWNS. The gentleman's time has expired.

Mr. LYNCH. It would have been disastrous to the American people.

Chairman TOWNS. The gentleman's time has expired. And I yield 2 minutes to the gentleman from Ohio, Mr. Jordan.

Mr. JORDAN. Thank you, Mr. Chairman.

Mr. Paulson, I want to clarify the chain of events surrounding the original request for the TARP dollars, original request to Congress. You came to the Congress, everyone on this committee, I think everyone in Congress, would admit you came to us in September and said, we need the money to buy troubled assets, toxic assets.

As everyone knows, at some point you changed your mind. When did you change your mind and decide you weren't going to purchase the troubled assets, you were going to inject capital into the banks? When did that happen?

Mr. PAULSON. I changed my mind. I came to Congress on September 18th.

Mr. JORDAN. Congress first voted it down. October 3rd, we voted for it. When did you change your mind?

Mr. PAULSON. It was our strategy when I came to Congress to buy illiquid assets, purchase illiquid assets.

Mr. JORDAN. When? We have 2 minutes. When did you change your mind?

Mr. PAULSON. Two weeks went on, and it was by the time——

Mr. JORDAN. Before the vote on October 3rd or after the vote? When did you change your mind?

Mr. PAULSON. I had begun considering putting capital into the banks as one option as we got near the final vote, but I had not changed my mind yet on the strategy. And I will say one other thing to you, right up even after we put capital in the banks, which we were forced to do by changing circumstances——

Mr. JORDAN. Did you change your mind before the vote or after the vote, because we have the interchange——

Mr. PAULSON. I changed my mind after the vote because I did not change—could I just say this? I did not change my mind on purchasing illiquid assets until mid to late October after we put the capital in.

Mr. JORDAN. Just so I am clear, you are saying you didn't change your mind until after the vote. I want to point to this, the book, David Wessel's book that came out, In The Fed We Trust, page 226, 227, and you have just been given a copy of what it says. The House of Representatives rejected the Bush administration's bank rescue plan on the 29th of 2008. The next morning, Mr. Paulson ran into Michele Davis, the spokeswoman and policy coordinator in the Treasury Building. "I think we are going to have to put equity in the banks," he said, despite what Paulson had told Congress, buying toxic assets was going to take too long. Davis gave him a blank stare, "we haven't even gotten the bill through Congress," she remembered thinking. "How are we going to explain this?" she told her boss. "We can't say that now." He took the advice.

So again, I am asking you, was it before or after, because you have said two different things. You said I started thinking about it, but you said I didn't make the decision until after, but you sold the Congress on the simple fact that you were going to buy the troubled assets. That is why they needed the money.

Mr. PAULSON. If you would let me——

Mr. JORDAN. And your spokesman directly contradicts that.

Mr. PAULSON. Congressman, let me answer the question. Give me a minute to answer the question.

During that period, when Congress was acting, the situation worsened considerably. As we got near the final vote, it was beginning to be clear to me that we were going to need to think through other options. But long after, even after we put capital in the banks, OK, even after——

Mr. JORDAN. Did you express that concern to the Congress?

Chairman TOWNS. The gentleman's time has expired.

Mr. PAULSON. Let me finish it. Even after we put capital in the banks, it was still my intent to proceed with an illiquid asset purchase program until we got into late October.

Mr. JORDAN. Let me ask you one question.

Chairman TOWNS. I am sorry, the gentleman's time is expired.

I now yield 2 minutes to the gentleman from Maryland, Mr. Van Hollen.

Mr. VAN HOLLEN. Thank you, Mr. Chairman.

Thank you, Mr. Paulson, and I accept your testimony that failure to act and to enact a financial rescue plan would have led to, as you said, economic disaster.

When you and President Bush came before the Congress in an emergency, you submitted a plan that did not include at the time a mechanism to make sure that the taxpayer would recoup any dollars that had been extended to the financial sector.

The Congress at that time inserted a provision requiring the President, whoever that President may be, to submit a plan to recover those funds on behalf of the taxpayer. President Obama has now done that in proposing a fee.

And my question to you is, do you agree that, given everything that taxpayer did to save the financial industry, that in addition to taking measures to prevent this from happening in the future, we should also make sure that we put in place a mechanism to recover the moneys that went to Wall Street and other financial banks as part of the rescue?

Mr. PAULSON. I do agree with that, but the provision that was put into the TARP legislation envisioned, contemplated looking at a 5-year window, and at the end of the 5-year time period, if the taxpayer hadn't recovered the money, then there was going to be a tax.

Now, today, as I look at the circumstance, the money is going to come back from the banks, in my judgment, with a profit to the taxpayer. And it is too early to tell about to what extent the money is going to come back from the rest of the program. I frankly think that the taxpayers will end up being pleasantly surprised and much more will come back.

So my only question about the tax that is being suggested is, is it too soon to make that judgment, No. 1. But most importantly, I don't want that to take our focus off of dealing with what is the real problem. We better fix this system so it doesn't happen again.

Mr. VAN HOLLEN. But would you agree there should be a mechanism in place to ensure that at the end of the day, the taxpayer recoups 100 percent of the TARP moneys?

Mr. PAULSON. Yes, that was the intent of Congress and I think that is the right thing to do. I agree.

Mr. VAN HOLLEN. Thank you. Thank you, Mr. Paulson.

Ms. NORTON [presiding]. Thank you, Mr. Paulson.

Mr. PAULSON. Madam Congresswoman.

Ms. NORTON. Yes?

Mr. PAULSON. I had agreed to stay for another 8 minutes. It has been 10 minutes.

Ms. NORTON. For that reason, I dismiss the gentleman who had the time to tell him his time had passed, and for the committee, and especially for Chairman Towns, may I thank you for not only 8 minutes, but 10 minutes.

Mr. PAULSON. Thank you. Thank you. [Laughter.]

Ms. NORTON. We would like to call the third panel.

Our final witnesses for today's hearing are Neil Barofsky, the Special Inspector General for TARP; Thomas Baxter, who is general counsel and executive vice president of the Federal Reserve Bank of New York; Elias Habayeb, the former chief financial officer of the Financial Services Group of AIG; and Stephen Friedman, the former chairman of the Board of Directors of the Federal Reserve Bank of New York, and current member of the Board of Directors of Goldman Sachs.

May I ask the witnesses to stand while I administer the oath?

[Witnesses sworn.]

Ms. NORTON. Let the record reflect that the witnesses have answered I the affirmative. You may now be seated.

I will ask the witnesses to summarize their testimony in 5 minutes. The yellow light means you have a minute left. The red light means stop.

And then, of course, we will have time for questions from Members.

All the witnesses have opening statements, so I believe that given the four votes, that Members will be back by the time your statements are done, for questions. I thank you.

Mr. Barofsky, would you present your testimony first?

STATEMENTS OF NEIL M. BAROFSKY, SPECIAL INSPECTOR GENERAL FOR THE TROUBLED ASSET RELIEF PROGRAM; THOMAS BAXTER, GENERAL COUNSEL AND EXECUTIVE VICE PRESIDENT, FEDERAL RESERVE BANK OF NEW YORK; ELIAS HABAYEB, FORMER SENIOR VICE PRESIDENT AND CHIEF FINANCIAL OFFICER, FINANCIAL SERVICES DIVISION, AMERICAN INTERNATIONAL GROUP, INC.; STEPHEN FRIEDMAN, FORMER CHAIRMAN, FEDERAL RESERVE BANK OF NEW YORK

STATEMENT OF NEIL M. BAROFSKY

Mr. BAROFSKY. Thank you, Madam Chair.

It is an honor to once again be back testifying before this committee. I would like to thank this committee for the support it has shown our office, as well as its leadership and tenacity in bringing about transparency to the AIG bailout generally, and in particular to the counterparty payments.

This past November we issued our audit, an audit that was requested by Representative Cummings and 26 other Members of Congress, including members of this committee, reporting on the decisionmaking process that led to then-President Geithner and the Federal Reserve making the decision, the choice to pay 100 cents on the dollar, effectively par value, for a series of securities that at the time were worth less than half of that amount.

And as we demonstrate in the audit, that was in fact a choice, a series of policy choices that were made that limited the ability of the Federal Reserve in its negotiations, and a choice to conduct the negotiations in the way that they did.

And in our audit and in our testimony, we lay out the different justifications and explanations given by the Federal Reserve, many of which Secretary Geithner repeated this morning, and our responses, and in some cases our criticisms of those policy decisions.

What I would like to focus on today, though, is expanding a different theme in the audit, and that is looking at the tone and the amount of effort that went into those negotiations, even assuming all those policy decisions which restricted the latitude of the Federal Reserve.

How are those negotiations conducted? Well, essentially a number of mid- and senior-level executives at the FRBNY reached out to their counterpart at AIG's counterparties. They did this basically over the telephone, and after informing them that even the negotiations themselves were voluntary, they asked if they would be willing to take a haircut on the amount of concession. For seven of the eight, the answer was "no." For the eighth, UBS, the answer was "yes" so long as the other counterparties also agreed to a similar concession.

The Federal Reserve at that point decided to shut down negotiations; not to pursue that willingness to negotiate; and decided with the approval of Secretary Geithner, to pay 100 cents on the dollar. Now, this stands in stark contrast to a negotiation that occurred just a few weeks earlier. And this, of course, was the negotiation by which the government purchased $125 billion of preferred securities from the nine largest institutions as part of the TARP's Capital Purchase Program. There, unlike in AIG, it was the principals that were involved: President Geithner, Secretary Paulson, and Chairman Bernanke on behalf of the government. And on behalf of the counterparties: the banks—some of the exact same banks that were subject to the AIG discussions—and the chief executive officers. There, unlike in AIG, the conversations weren't conducted over the telephone. Each of those CEOs was summoned to Washington and told to appear in a Treasury conference room, gathered together. And there, unlike in AIG, the message was forceful. President Geithner, Chairman Bernanke, Secretary Paulson and others, made it very clear of the importance that they believed that this negotiation was; how important it was for the banks to agree. They used the terms like "that it would be good for the country for them to do so."

No such similar effort was taken with respect to the AIG negotiations, and the result of the Capital Purchase Program: 100 percent agreement. The result of the AIG, as we all know, were failed negotiations.

Now, would it have made a difference if President Geithner or Secretary Paulson got on the phone and talked to those chief executive officers? Would it have resulted in the savings of billions or tens of billions of dollars for the taxpayer? We don't know. We can't know. But we do know, because we have recently been informed by the French regulator, the same regulator that the Federal Reserve cited their intransigence as being one of the great barriers to achieving effective negotiated haircuts, that recently told SIGTARP that in fact they would have been willing to engage in just such a negotiation, so long as it was at a very high level, so long as it was completely transparent, and as long as it was universal agreement, everyone came around the table.

And we also know that if such negotiations occurred and were successful, they would have addressed all of the concerns that Secretary Geithner addressed this morning, and many of the concerns that are outlined in our audit of concerns by the Federal Reserve. But we will never know because that effort was simply not taken.

Madam Chair, our audit covers, I see my time is running low, our audit obviously covers a lot of other issues, as does our testimony, including some of the recent troubling comments from Treasury that impact transparency, and of course, I will be available to answer any questions that you or other Members of the committee may have.

Thank you.

[The prepared statement of Mr. Barofsky follows:]

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STATEMENT OF NEIL BAROFSKY

SPECIAL INSPECTOR GENERAL
FOR THE TROUBLED ASSET RELIEF PROGRAM

BEFORE THE
HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

January 27, 2010

Chairman Towns, Ranking Member Issa, and Members of the Committee, I am honored to appear before you today to discuss SIGTARP's audit examining the factors affecting efforts to limit payments to American International Group ("AIG") counterparties that was released back in November,[1] as well as to discuss several troubling issues that have come to light since the audit was released that relate to whether the Government has been fully transparent with the American people with respect to the AIG transactions.

Before I begin, I would like to thank the Committee for both its strong support and its leadership on this issue. SIGTARP's audit was commenced as the result of a letter request made by Congressman Cummings and 26 other Members of Congress, including several members of this Committee, and the tenacity and leadership demonstrated by the Chairman, Ranking Member and many other members of this Committee has been crucial in continuing the drive for transparency and accountability on the AIG bailout in general and the counterparty payments in particular.

FACTUAL BACKGROUND

In September 2008, AIG was on the brink of collapse, unable to access credit in the private markets and bleeding cash. On September 16, 2008, the Federal Reserve Bank of New York ("FRBNY"), pursuant to the authorization of the Board of Governors of the Federal Reserve System ("Federal Reserve Board," and, collectively with FRBNY, "Federal Reserve") provided AIG with an $85 billion loan. On November 10, 2008, the Federal Reserve and the Department of the Treasury ("Treasury") announced the restructuring of the Government's financial support to AIG. As part of this restructuring, the Federal Reserve Board authorized FRBNY to lend up to $30 billion to Maiden Lane III, a newly formed limited liability company. Pursuant to this authorization, FRBNY lent $24.3 billion to Maiden Lane III, which, in

[1] A copy of the audit is appended hereto for the Committee's reference.

combination with a $5 billion equity investment from AIG, was used to fund the purchase of assets from counterparties of American International Group Financial Products ("AIGFP") having a fair market value of about $27.1 billion. In exchange for that payment and being permitted to retain $35 billion in collateral payments that had been previously made by AIG (including billions in collateral payments made possible by the FRBNY loan), the counterparties agreed to terminate their credit default swap contracts—insurance-like contracts intended to protect the underlying assets—with AIGFP. Because the counterparties were both paid the fair market value of the assets underlying the credit default swap contracts and permitted to keep the collateral that had previously been posted; the counterparties were effectively paid the par value of the underlying assets.

In light of this factual context, and consistent with the issues raised by Congressman Cummings and others, SIGTARP's audit addressed (1) the decision-making processes leading up to the creation of Maiden Lane III, (2) why AIG's counterparties were paid effectively at par value, and (3) AIG's current exposure to credit default swaps outside Maiden Lane III.

SIGTARP'S AUDIT FINDINGS

SIGTARP's audit, which was issued on November 17, 2009, found that, when first confronted with the liquidity crisis at AIG, the Federal Reserve Board and FRBNY, who were then contending with the demise of Lehman Brothers, turned to the private sector to arrange and provide funding to stave off AIG's collapse. Confident that a private sector solution would be forthcoming, FRBNY did not develop a contingency plan, and, when private financing fell through, FRBNY was left with little time to decide whether to rescue AIG and, if so, on what terms. Having witnessed the dramatic economic consequences of Lehman Brothers' bankruptcy just hours before, senior officials at the Federal Reserve and Treasury determined that an AIG bankruptcy would have far greater systemic impact on the global financial system than Lehman's bankruptcy and decided to step in to prevent that result.

Not preparing an alternative to private financing, however, left FRBNY with little opportunity to fashion appropriate terms for the support, and, believing it had no time to do otherwise, it essentially adopted the term sheet that had been the subject of the aborted private financing discussions (an effective interest rate in excess of 11 percent and an approximate 80 percent ownership interest in AIG), albeit in return for $85 billion in FRBNY financing rather than the $75 billion that had been contemplated for the private deal. In other words, the decision to acquire a controlling interest in one of the world's most complex and most troubled corporations was done with almost no independent consideration of the terms of the transaction or the impact that those terms might have on the future of AIG.

The impact of those terms, however, soon became apparent to FRBNY. In a matter of days, FRBNY officials recognized that, although the $85 billion credit line permitted AIG to meet billions of dollars of collateral calls and thus avoid an immediate bankruptcy, its terms were unworkable. Among other things, the interest rate imposed upon AIG was so onerous that, if unaddressed, the burden of servicing the FRBNY financing greatly increased the likelihood that there would be further credit rating downgrades for AIG, a result that FRBNY officials believed would have "devastating" implications for AIG. For this and other reasons, modification of the original terms thus became inevitable. One example of such modification was Treasury's $40 billion investment in AIG in November 2008 through the Troubled Asset Relief Program ("TARP") — which was used to pay down the FRBNY loan in part. Another was termination of a portion of AIG's credit default swap obligations made possible through the creation of Maiden Lane III.

A significant cause of AIG's liquidity problems stemmed from its obligations to post collateral (cash payments that equaled the drop in value of the underlying securities) in connection with AIGFP's credit default swap contracts. To avoid the necessity for AIG to continue to post collateral and to reduce the danger of further rating agency downgrades, by early November 2008, FRBNY decided to create Maiden Lane III, a special purpose vehicle, to retire a portion of AIG's credit default swap portfolio by purchasing the underlying CDOs from the swap counterparties, which eased pressure on FRBNY's credit line and transferred the issues with these contracts off of AIG's balance sheet and on the Federal Reserve's.

When considering the amount of payment for the underlying CDOs for the Maiden Lane III transaction, FRBNY decided to attempt to seek concessions, or "haircuts," from the counterparties. FRBNY contacted by telephone eight of AIG's largest counterparties over a two-day period and attempted to obtain such concessions from the counterparties. Although one counterparty, UBS, was willing to make a modest 2 percent concession if the other counterparties did so, FRBNY's attempts to obtain concessions from the others were completely unsuccessful, and FRBNY decided to pay the counterparties the full market value of the CDOs, which, when combined with the already posted collateral, meant that the counterparties were effectively paid full face (or par) value of the credit default swaps, an amount far above their market value at the time.

On November 7th, 2008, FRBNY employees involved with the negotiations reported to then-FRBNY President Geithner on the efforts to convince AIG counterparties to accept haircuts on their claims against AIG in return for unwinding the CDS contracts. Noting both the willingness of UBS to negotiate a small haircut and the generally negative reactions from the other counterparties, these FRBNY officials recommended that FRBNY cease negotiations and proceed with paying the counterparties the market value of their underlying CDOs and permitting them to keep the collateral already posted, effectively paying them par for securities that collectively had a market value, based on the amount of the collateral payments, of approximately 48 cents on the dollar. According to these FRBNY executives, then-President Geithner "acquiesced" to the executive's proposal. When asked by SIGTARP if the executives felt they had received their "marching orders" from then-FRBNY President Geithner to pay the counterparties par, one FRBNY official responded "yes, absolutely."

The decision to pay effective par value was then brought before the Board of Governors of the Federal Reserve, which gave its approval. According to the General Counsel for FRBNY, officials from Treasury were not involved in the negotiations of concessions with AIG's credit default swap counterparties. The Chief Compliance Officer for Treasury's Office of Financial Stability at the time also told SIGTARP that Treasury was not involved with the Maiden Lane III transaction and, when asked about who at Treasury SIGTARP should speak with regarding the transactions, he responded that Secretary Geithner was the appropriate official.

In pursuing the counterparty negotiations, FRBNY made several policy decisions that severely limited its ability to obtain concessions. FRBNY officials told SIGTARP that: FRBNY determined that it would not treat the counterparties differently, and, in particular, would not treat domestic banks differently from foreign banks — a decision with particular import in light of what FRBNY officials recounted was the reaction of the French bank regulator which, according to FRBNY, refused to allow two French bank counterparties to make concessions; FRBNY refused to use its considerable leverage as the regulator of several of these institutions to compel haircuts because FRBNY was acting on behalf of AIG (as opposed to in its role as a regulator); FRBNY was uncomfortable interfering with the sanctity of the counterparties' contractual rights with AIG, which entitled them to full par value; FRBNY felt ethically restrained from threatening an AIG bankruptcy because it had no actual plans to carry out such a threat; and FRBNY was concerned about the reaction of the credit rating agencies should imposed haircuts be viewed as FRBNY backing away from fully supporting AIG. Although these were certainly valid concerns, these policy decisions came with a cost — they led directly to a negotiating strategy with the counterparties that even then-FRBNY President Geithner acknowledged had little likelihood of success.

FRBNY's decision to treat all counterparties equally (which FRBNY officials described as a "core value" of their organization), for example, gave each of the major counterparties effective veto power over the possibility of a concession from any other party. This approach left FRBNY with few options, even after one of the counterparties indicated a willingness to negotiate concessions. It also arguably did not account for significant differences among the counterparties, including that some of them had received very substantial benefits from FRBNY and other Government agencies through various other bailout programs (including billions of dollars of taxpayer funds through TARP), a benefit not available to some of the other counterparties (including the French banks). It further did not account for the benefits the counterparties received from FRBNY's initial bailout of AIG, without which they would have likely suffered far reduced payments as well as the indirect consequences of a potential systemic collapse. It also did not recognize that each bank's portfolio of assets were different and had different market values, meaning that certain counterparties (such as Goldman Sachs, the market value of whose securities, based on the collateral payments made by AIG, was approximately 40 cents on the dollar) arguably received a greater benefit than others (such as UBS, whose securities had a comparable market value of approximately 66 cents on the dollar).

Similarly, the refusal of FRBNY and the Federal Reserve to use their considerable leverage as the primary regulators for several of the counterparties, including the emphasis that their participation in the negotiations was purely "voluntary," made the possibility of obtaining concessions from those counterparties extremely remote. While there can be no doubt that a regulators' inherent leverage over a regulated entity must be used appropriately, and could in certain circumstances be abused, in other instances in this financial crisis regulators (including the Federal Reserve) have used overtly coercive language to convince financial institutions to take or forego certain actions. As SIGTARP reported in its audit of the initial Capital Purchase Program investments, for example, Treasury and the Federal Reserve fully used their leverage as regulators, just weeks before the negotiations with AIG's counterparties, to persuade nine of the largest financial institutions (including some of AIG's counterparties) to accept $125 billion of TARP funding. In stark contrast to those negotiations, in the case of the AIG counterparty payments, Mr. Geithner and Mr. Bernanke did not participate; nor did the CEO's of the counterparties; and the counterparties were not gathered together and told that they should, together, voluntarily concede to concessions because of the importance of this issue to the United States government. Instead, the negotiations were generally conducted through a series of telephone calls from executives at FRBNY to executives at the counterparties. Ultimately, in the CPP negotiations, there was no need for the Federal Reserve to impose the CPP investments on the participants using its regulatory authority because it obtained voluntary agreements based on an aggressive negotiating strategy. It is impossible to determine now, given the policy choices made by the FRBNY, whether a similarly proactive strategy with the AIG counterparties would have resulted in taxpayer savings.

Moreover, subsequent to the issuance of the audit report, SIGTARP was informed that the French regulator was in fact open to further negotiations with the Federal Reserve to discuss the possibility of such concessions. While they viewed the transactions proposed by the Federal Reserve as being violative of French law, the regulators informed SIGTARP that they believed that an exception was possible and that they were willing to further discuss potential concessions. The French regulators noted that such negotiations would have been unprecedented, would have likely required universal agreement among counterparties to make concessions, and would have had to be conducted in a transparent manner and at a high level, but that continued negotiations were possible. While the French regulators would not clarify to SIGTARP what specific statements were made to the Federal Reserve during the actual negotiations, they did inform SIGTARP that they did not "slam the door" to such continued discussions.

Questions have been raised as to whether the Federal Reserve intentionally structured the AIG counterparty payments to benefit AIG's counterparties — in other words that the AIG assistance was in effect a "backdoor bailout" of AIG's counterparties. Then-FRBNY President Geithner and FRBNY's general counsel deny that this was a relevant consideration for the AIG transactions. Irrespective of their stated intent, however, there is no question that the *effect* of FRBNY's decisions — indeed, the very *design* of the federal assistance to AIG — was that tens of billions of dollars of Government money was funneled inexorably and directly to AIG's counterparties. Although the primary intent of the initial $85 billion loan to AIG may well have been to prevent the adverse systemic consequences of an AIG failure on the financial system and the economy as a whole, in carrying out that intent, it was fully contemplated that such funding would be used by AIG to make tens of billions of dollars of collateral payments to the AIG counterparties. The intent in creating Maiden Lane III may similarly have been the improvement of AIG's liquidity position to avoid further rating agency downgrades, but the direct effect was further payments of nearly $30 billion to AIG counterparties, albeit in return for assets of the same market value. Stated another way, by providing AIG with the capital to make these payments, Federal Reserve officials provided AIG's counterparties with tens of billions of dollars they likely would have not otherwise received had AIG gone into bankruptcy.

Any assessment of the costs of these decisions to the Government and the taxpayer necessarily must look beyond FRBNY's loan to Maiden Lane III to also take into account both the funds that FRBNY previously loaned to AIG and the subsequent TARP investments. All of these infusions to AIG are linked inextricably: more than half the total amounts paid to counterparties in connection with the credit default swap portfolio retired through Maiden Lane III did not come about through the Maiden Lane III CDO purchases, but rather from AIG's earlier collateral postings that were made possible in part by the original FRBNY loan, which was, in turn, paid down with TARP funds. Because of this linkage, the ultimate costs to the Government and the taxpayer cannot be measured in isolation. Stated another way, irrespective of whether FRBNY is made whole on its loan to Maiden Lane III, we will only be able to determine the ultimate value or cost to the taxpayer after the likelihood of AIG repaying all of its assistance can be more readily determined.

The remarkable narrative surrounding the AIG loans and the creation of Maiden Lane III set forth in SIGTARP's audit gives rise to two additional lessons learned. First, AIG stands as a stark example of the tremendous influence of credit rating agencies upon financial institutions and upon Government decision making in response to financial crises. In the lead-up to the crisis, the systemic over-rating of mortgage-backed securities by rating agencies was reflected in the similarly over-rated CDOs that underlied AIGFP's credit default swaps. Once the financial crisis had come to a head, the credit rating agencies' downgrades of AIG itself and of the underlying securities played a significant role in AIG's liquidity crisis as those downgrades and the related market declines in the securities required AIG to post billions of dollars in collateral. The threat of further rating agency downgrades due to the onerous terms of the initial FRBNY financing, among other things, led to further Government intervention, including the TARP investment in AIG and the necessity to do something with the swap portfolio, *i.e.*, Maiden Lane III. And the concern about the reaction of the credit rating agencies played a role in FRBNY's decision not to pursue a more aggressive negotiating policy to seek concessions from counterparties. All of these profound effects were based upon the judgments of a small number of private entities that operate, as described in SIGTARP's October 2009 Quarterly Report to Congress, on an inherently conflicted business model and that are subject to minimal regulation. Without drawing any conclusions about the particular actions taken by the rating agencies in the case of AIG, this report further demonstrates the dramatic influence of these entities on our financial system.

Second, the now familiar argument from Government officials about the dire consequences of basic transparency, as advocated by the Federal Reserve in connection with Maiden Lane III, once again simply does not withstand scrutiny. Federal Reserve officials initially refused to disclose the identities of the counterparties or the details of the payments, warning that disclosure of the names would undermine AIG's stability, the privacy and business interests of the counterparties, and the stability of the markets. After public and Congressional pressure, AIG disclosed the identities. Notwithstanding the Federal Reserve's warnings, the sky did not fall; there is no indication that AIG's disclosure undermined the stability of AIG or the market or damaged legitimate interests of the counterparties. The lesson that should be learned — one that has been made apparent time after time in the Government's response to the financial crisis — is that the default position, whenever Government funds are deployed in a crisis to support markets or institutions, should be that the public is entitled to know what is being done with Government funds. While SIGTARP acknowledges that there might be circumstances in which the public's right to know what its Government is doing should be circumscribed, those instances should be very few and very far between.

ONGOING TRANSPARENCY ISSUES

Since the release of the audit, three broad issues have come to light that call into question whether the Government has been and is being as transparent as possible with the American people.

The first relates to public statements recently made by Treasury about the AIG transactions. For example, on January 7, 2010, in response to press inquiries regarding the role of Secretary Geithner in the decisions concerning AIG, a Treasury spokesperson stated the following via email to reporters:

> In the transaction at the heart of this dispute (Maiden Lane III's purchase of CDO's), the FRBNY made a loan of $25 billion which is on track to be paid back in full with interest *so that taxpayers will be made whole*. Somehow that fact that the government's loan is "above water" gets lost in all the consternation despite its mention on page 2 of the SIG-TARP report and weekly updates on the FRBNY's web site. (Emphasis added.)

This statement simply does not advance the cause of transparency. As noted in the audit, it is clear that all of the infusions to AIG are linked: more than half the total amounts paid to counterparties in connection with the swap portfolio retired through Maiden Lane III did not come about through the Maiden Lane III purchases, but rather from AIG's earlier collateral postings that were made possible in part by the original $85 billion FRBNY loan; that loan, in turn, was paid down with $40 billion of TARP funds. Treasury's own TARP financial statement estimates that Treasury will *not* be made whole, but is rather projected to lose more than $30 billion on its AIG investments. Again, the various AIG infusions are directly linked: (a) the counterparties terminated their credit default swap agreements with AIG after they were *both* paid the fair market value of the underlying assets through Maiden Lane III and permitted to keep the collateral payments made by AIG; (b) many of those collateral payments were only made possible by the FRBNY loan; and (c) that loan was paid back in part by the initial $40 billion TARP investment. Narrowly asserting that taxpayers will be "made whole" on Maiden Lane III — just one part of the AIG counterparty transactions — without mentioning the huge losses Treasury expects to suffer on other, inextricably linked parts of *the very same* transactions is simply unacceptable; the American people deserve better.

The second issue relates to a series of documents that have recently been disclosed — as the direct result of the tenacity of the members of this Committee — about the Maiden Lane III transactions. As has been widely reported, these newly disclosed documents, among other things, relate to discussions about the public disclosure by AIG of the Maiden Lane III transactions in filings with the Securities and Exchange Commission. In light of these documents, we have initiated an investigation into whether there was any misconduct relating to the disclosure or lack thereof concerning the Maiden Lane III transactions.

Third, additional documents and facts have come to light that have caused SIGTARP to initiate an investigation to review the extent of the Federal Reserve's cooperation with SIGTARP during the course of the audit. For example, in connection with the recent document productions to this Committee, documents have come to light that were not provided to the SIGTARP audit team during the course of the audit. FRBNY's outside counsel has told SIGTARP that FRBNY will cooperate fully with SIGTARP's investigation.

With respect to these investigations, it is SIGTARP's policy not to comment publicly on non-public, ongoing criminal or civil investigations, and thus we cannot comment further at this time, other than to note that these assertions do not at this time constitute a factual finding by SIGTARP. At the conclusion of the investigations, however, we anticipate that the details of our findings will be reported to Congress, as appropriate, either through formal court filings or in the form of Investigative Reports.

Chairman Towns, Ranking Member Issa and Members of the Committee, I want to thank you again for this opportunity to appear before you, and I would be pleased to respond to any questions that you may have.

Ms. NORTON. Thank you, Mr. Barofsky.

Mr. Baxter, we would like you to go next.

STATEMENT OF THOMAS C. BAXTER

Mr. BAXTER. Good afternoon, Madam Chairman Norton, Ranking Member Issa, and other Members of this committee. Thank you for inviting me to appear here today.

As the general counsel of the Federal Reserve Bank of New York, I welcome the opportunity to talk about the Federal Reserve's work to stabilize AIG at a critical point. I will also address the role played by the Federal Reserve Bank of New York in securities disclosures made by AIG.

Let me begin with just a few words about autumn 2008, when our Nation was challenged by a financial crisis of a kind we had not seen since the Great Depression. At the New York Fed, we were literally working around the clock trying to implement a number of liquidity programs directed toward market stability.

Today, we consider some of the actions taken during those frenetic times with respect to AIG. Everything we have done since this crisis began has been with the goal of stabilizing our financial system and assisting our economic recovery.

Turning to September 2008, and the actions taken by the New York Fed, the Board of Governors of the Federal Reserve System, and the Department of the Treasury, they were designed to avoid the catastrophic systemic consequences that would have resulted from an AIG bankruptcy. Every American would have been adversely impacted. We did not lend to AIG because we wanted to, but because we had to. A decision not to act might have been easier on us, but it would have been worse for all.

Now, I will turn to the specific issues that bring me here today. First, there have been concerns about AIG's counterparties receiving large payments for terminating CDS contracts and selling collateralized bid obligations. There have been allegations that this was a backdoor bailout designed by the Federal Reserve to assist the banks at the expense of the American taxpayer.

These allegations are not true. AIG was scheduled to announce an earnings loss of nearly $25 billion on November 10, 2008. Had we not reached agreement with the counterparties to terminate their credit default swap contracts by that date by acquiring the CDOs, AIG would have been downgraded by the credit rating agencies and thrown once again to the brink of bankruptcy. This would have returned us to the situation we faced in September and required even further government support. We took the action needed to terminate the CDS contracts by the deadline, and our focus was on solving the AIG liquidity problem, not on benefiting AIG's counterparties.

Second, I would like to clarify the misunderstanding that the Federal Reserve and Treasury Department received nothing of value in exchange for the payments to AIG's counterparties. As part of the termination deal, the Federal Reserve, through its special purpose vehicle, Maiden Lane III, paid approximately $29 billion and received assets with a fair market value of $29 billion. The par value of the assets was approximately $62 billion. Today, the value of the assets which secure the Federal Reserve's loan exceeds our loan balance by several billion dollars.

Third, concerns have been expressed about our involvement in AIG's securities disclosures. In particular, there have been allegations that we somehow tried to engage in a cover-up by recommending that AIG strike certain sentences in its SEC disclosures related to the payments to the counterparties. These allegations are not true. Our sole purpose was to ensure that securities law disclosures by AIG were accurate and appropriately protective of taxpayer interests.

Let me finish by thanking the committee for holding this hearing. We submitted an extensive statement yesterday and we have delivered 250,000 pages of documents to you. I believe that upon careful examination, the committee will see that our actions successfully addressed a potentially calamitous risk to the economy, and in doing so, protected the interests of the American people.

[The prepared statement of Mr. Baxter follows:]

Embargoed until
10:00 a.m. EDT
January 27, 2010

Statement by

Thomas C. Baxter, Jr.

Executive Vice President and General Counsel, Federal Reserve Bank of New York

before the

Committee on Government Oversight and Reform

United States House of Representatives

regarding

Factors Affecting Efforts to Limit Payments to AIG Counterparties

January 27, 2010

Good morning, Chairman Towns, Ranking Member Issa, and other members of the Committee. Thank you for inviting me to testify today. As the General Counsel of the Federal Reserve Bank of New York, I welcome the opportunity to talk about the Federal Reserve's work to stabilize AIG, and more specifically the Federal Reserve's restructuring of certain problematic AIG contracts in November of 2008, at a critical point in what is aptly characterized as the worst financial crisis since the Great Depression. I will also speak about the role played by the Federal Reserve Bank of New York (the "New York Fed") in securities disclosures made by AIG over the following months. The actions of the New York Fed and the Board of Governors of the Federal Reserve System (the "Board of Governors") in stabilizing AIG were undertaken to avoid the potentially catastrophic consequences that would have resulted from an AIG bankruptcy.

Stabilizing AIG

I. Background

As is now well known, AIG's liquidity crisis emerged at nearly the same time that the securities firm Lehman Brothers collapsed, one week after the GSEs Fannie Mae and Freddie Mac were placed in conservatorship, and amidst ongoing acute stress in U.S. and global financial markets. It was against this backdrop, and in recognition of the financial stability threat posed by the abrupt and disorderly failure of an even larger and more complex firm than the one that had failed a day earlier, that the Board of Governors, with the full support of the Treasury Department, decided to intervene to prevent the bankruptcy of AIG on September 16, 2008.

AIG was a $1 trillion company when it alerted the Treasury and the Federal Reserve that it was encountering severe liquidity problems. It remains one of the largest insurance and financial services companies in the world. AIG conducts insurance and finance operations in more than 140 countries and has more than 76 million individual and corporate customers globally. In the United States, AIG has approximately 30 million customers, including commercial, institutional and individual customers. It is also a major provider of protection to municipalities, pension funds, and other public and private entities through guaranteed investment contracts and products that protect participants in 401(k) retirement plans.

In terms of net premiums underwritten, AIG is both the largest life and health insurer, and the second largest property and casualty insurer in the United States. It has written more than 81 million life insurance policies worldwide, with a face value of $1.9 trillion. The company insures approximately 180,000 small businesses, non-profit organizations, and other corporate entities. Estimates are that close to one-third of the United States population, or 106 million people, are employed by entities that are protected by insurance coverage issued by AIG. AIG is the largest issuer of fixed annuities in the United States. It is also one of the largest providers of retirement services to non-profit healthcare groups, schools and universities. More than six million people hold retirement plans or accounts with AIG.

AIG had also been a major participant in derivatives markets through its Financial Products business unit ("AIG FP"), an unregulated subsidiary. AIG FP had engaged in financial transactions with a broad range of customers, which include many major national and international financial institutions, as well as U.S. pension plans, stable value funds, and municipalities.

An AIG bankruptcy under the economic conditions existing in the fall of 2008 would have had catastrophic consequences for our financial system and our economy. Money market mutual funds to which so many Americans entrust their savings were major holders of the roughly $20 billion of commercial paper issued by AIG. Losses to these funds would have had potentially devastating effects on confidence and would have accelerated the run on financial institutions of all kinds. By way of comparison, money market mutual funds and other investors held approximately $5 billion of commercial paper issued by Lehman Brothers. Lehman's collapse triggered a run on money market funds after the Reserve Primary Fund "broke the buck" due to losses on Lehman commercial paper.

Global commercial banks and investment banks would have suffered losses on loans and lines of credit to AIG and on derivatives contracts and other transactions with AIG FP. This could have led to the outright collapse of the financial system. At a minimum, it would have caused even greater constraints on the availability of credit to homeowners and businesses.

In the event of an AIG failure, many of AIG's insurance subsidiaries likely would have been seized by their state and foreign regulators, leaving U.S. policyholders facing considerable uncertainty about their rights and claims. State and local government entities that had lent in excess of $10 billion to AIG would have been exposed to losses in an already difficult and deteriorating municipal budget environment.

AIG also had approximately $38 billion of what are called stable value wrap contracts. These contracts allow trustees and investment managers of defined contribution plans to manage the asset-liability mismatch arising from withdrawals. Workers whose 401(k) plans had purchased these contracts from AIG to insure against the risk that their stable value funds would decline in value could have seen that insurance disappear in the event of an AIG bankruptcy. Pension plans would have been forced to write down their assets from book to market value, resulting in significant losses in participants' portfolios.

Ultimately, AIG, the world's largest insurance company, received extraordinary assistance because of the impact its failure would have had all across America. As Federal Reserve Vice Chairman Donald Kohn has testified, "because of the dependence of modern economies on the flow of credit, serious financial instability imposes disproportionately large costs on the broader economy. The rationale for public investment in the financial industry is not, therefore, any special regard for managers, workers, or investors in that industry over others, but rather the need to prevent a further deterioration in financial conditions that would destroy jobs and incomes in all industries and regions."

II. AIG Credit Facilities

On September 16, 2008 the Board of Governors authorized the New York Fed to lend up to $85 billion to AIG through a secured revolving credit facility ("Fed Facility"). The Fed Facility was (and remains) secured by a pledge of a substantial portion of AIG's assets, including ownership interests in the company's domestic and foreign insurance subsidiaries. As additional compensation for this Facility, AIG issued, to a trust for the benefit of the Treasury, preferred stock convertible into approximately 78 percent of AIG's outstanding common stock.

The policy decision to authorize a loan to AIG was a difficult one, because addressing the systemic crisis facing the United States required the Federal Reserve to assist a private company at the center of the risks that led to the crisis. Nonetheless, the potentially far-reaching consequences of an AIG bankruptcy compelled policymakers to take affirmative action. The failure of AIG in the fall of 2008 would have imposed significant financial losses on many individuals, households and businesses, shattered confidence in already fragile financial markets, and greatly increased fear and uncertainty about the viability of our financial institutions. Last month, Chairman Bernanke observed that the Federal Reserve did not lend support to AIG for the Fed's own benefit, "because it obviously has hurt the Federal Reserve in the public's view. We did it because we felt that there was no other way to avoid what [many] have called the risk of a catastrophic collapse of the financial system."

The initial emergency $85 billion Fed Facility was successful in stabilizing AIG in the short term, but the company's financial condition and capital structure remained vulnerable to further deterioration in market conditions. AIG's pressing liquidity needs were resulting in rapid and sizeable draws on the Fed Facility, prompting concern that AIG's needs might well exceed the facility's capacity. The prospect of further downgrades of AIG's credit rating by rating agencies intensified the liquidity concerns AIG faced, because such downgrades would have immediately triggered billions of dollars of additional liquidity demands related to AIG FP's business. Absent further government action, a ratings downgrade was all but inevitable.

In early October of 2008, the Board of Governors approved an additional secured credit facility that permitted the New York Fed to lend AIG up to $37.8 billion in order to address liquidity needs related to the securities lending program of certain AIG domestic insurance subsidiaries. Additionally, toward the end of October 2008, four AIG affiliates began participating in the Federal Reserve's Commercial Paper Funding Facility ("CPFF") on the same terms and conditions as other participants.

Notwithstanding AIG's access to these additional Federal Reserve credit facilities, AIG continued to face serious liquidity pressures. Some of these pressures arose out of AIG's losses on residential mortgage backed securities ("RMBS") it had invested in as part of its securities lending program. In November 2008, the Board of Governors authorized the New York Fed to take a second step to alleviate these pressures by funding Maiden Lane II, which purchased RMBS at market value and allowed AIG to unwind its securities lending transactions. With this transaction, the original $37.8 billion facility to fund AIG's repayment of its securities lending transactions was fully repaid and terminated.

A substantial additional cause of AIG's liquidity pressure was its exposure to credit default swaps, or CDSs, one of many derivative products AIG FP offered. A CDS is essentially an unregulated insurance policy that protects the holder of a security from default. AIG FP, the CDS seller, agreed to protect its counterparties, the CDS buyers, from losses incurred on certain securities owned by the counterparties. In return, the counterparties paid AIG FP periodic premiums.

Under the terms of these particular CDS contracts, counterparties had the right to require AIG FP to post cash collateral as a result of adverse events relating either to the underlying securities, which in this case were multi-sector collateralized debt obligations ("CDOs"), or to AIG's credit condition, such as a ratings downgrade. The posted collateral secured each counterparty in the event AIG FP was not able to perform on the contract as contemplated. AIG FP's performance on these contracts was also guaranteed by its parent, AIG, making it impossible to isolate AIG FP's problems from AIG or its insurance subsidiaries. As AIG's financial condition deteriorated in 2008, and as the CDOs declined in value as the nation fell deeper into crisis, AIG FP was forced to post more and more collateral to the counterparties, a cash outflow that in turn caused AIG's liquidity and credit condition to deteriorate further. It was a vicious cycle.

As explained in the report by the Office of the Special Inspector General for the Troubled Asset Relief Program, or SIGTARP, entitled "Factors Affecting Efforts to Limit Payments to AIG Counterparties" (SIGTARP-10-003), the Federal Reserve considered a number of options in an effort to address the liquidity drain created by AIG's CDS exposure. One critical constraint applied to any option chosen: it had to be arranged by the earnings announcement on November 10th, when AIG was facing an imminent credit ratings downgrade in connection with its announcement of a $25 billion loss for the third quarter.

The first proposed option would have allowed the counterparties to keep their multi-sector CDOs and the protection provided by the credit default swaps. The counterparties would have agreed to forego additional collateral calls in exchange for a New York Fed guarantee of AIG's performance under the credit default swaps. Under this proposal, the New York Fed would not own the underlying CDOs, but the New York Fed – through the guarantee – would eliminate the downside risk to the counterparties of a further decline in the CDOs' market value. Not only did this structure have unappealing economics – taxpayer funds would have been exposed to the downside risk with no opportunity to participate in the upside – it also was not viable because the Federal Reserve lacked legal authority to issue the proposed guarantee under this structure.

The second proposed option would have involved persuading AIG's counterparties to take back some of the risk relating to the CDOs from AIG by canceling their credit default swaps and selling the underlying CDOs to an SPV. The SPV would be funded by the counterparties, the New York Fed, and AIG, with the counterparties' interests subordinated to those of the New York Fed. The New York Fed was concerned that the counterparties would not be motivated to cancel the swaps if they were left with un-hedged CDO risk associated with their part of the financing. This option was also deemed impractical because the complex negotiations required for each counterparty could not be completed quickly enough to satisfy AIG's liquidity needs, i.e., before November 10th.

The third option became Maiden Lane III.

III. Maiden Lane III

In the months leading up to early November 2008, AIG had been actively engaged in efforts to negotiate tear-ups of its CDS contracts with its counterparties. AIG was completely unsuccessful. The need for the tear-ups was real; AIG was effectively hemorrhaging cash. Throughout October, while the New York Fed worked to identify various restructuring options, AIG continued to negotiate with its counterparties. The New York Fed ultimately agreed to participate in these counterparty negotiations, extremely mindful of the exigency of obtaining final agreement with at least the eight largest counterparties by Monday, November 10th, when earnings were to be released by AIG.

The earnings release would show a third quarter loss of approximately $25 billion. The ratings agencies had advised AIG that, absent a parallel announcement of solutions to its liquidity problems, a ratings downgrade was certain following the earnings announcement. With that further downgrade, additional collateral calls, and possibly terminations, would be triggered. As of November 6, 2008, AIG had drawn down approximately $61 billion of the $85 billion Fed Facility, leaving $24 billion of liquidity for operations and further collateral calls. Continuing to borrow from the Fed Facility, however, was not a solution to AIG's problems. First, additional borrowing from the Federal Reserve would significantly add to AIG's overall debt burden, which was a very negative factor in the eyes of the rating agencies. Second, it was doubtful that the remaining $24 billion in the line of credit would cover the anticipated collateral calls under the CDS contracts and AIG's other liquidity needs.

In the limited time available, agreement had to be obtained from at least the eight largest counterparties, who together represented the bulk of AIG's CDS exposure. A ratings downgrade on November 10th would have created a possibly fatal downward spiral for AIG. Unless the Federal Reserve was prepared to pump substantially more funds into AIG by increasing the $85 billion credit line, the only option would have been to reverse course and allow AIG to file for bankruptcy. This abrupt reversal of course would not only have triggered all of the adverse consequences for the U.S. and global economies that prompted the initial intervention, it would also have undermined the public's trust in the U.S. government's commitment to the broader range of extraordinary financial stability initiatives underway during that very fragile period. With bankruptcy not an option, it was necessary to find a solution that stemmed the liquidity drain arising from the continuing collateral calls on the CDS contracts, stabilized AIG, and protected the taxpayer interests. The Maiden Lane III transaction was that solution.

In this context, the Board of Governors authorized the New York Fed to lend Maiden Lane III up to $30 billion, and to secure that loan with the multi-sector CDOs that were insured by the AIG CDS contracts. Pursuant to this authorization, the New York Fed lent $24.3 billion to Maiden Lane III that it used, in combination with a $5 billion equity investment from AIG, to purchase CDOs from 16 of AIG's counterparties. At the time, the CDOs had a fair market value of about $29.6 billion and a par value of approximately $62 billion. In exchange for agreeing to terminate AIG's CDS contracts and turning over the underlying CDOs to Maiden Lane III, the counterparties would also be allowed to retain approximately $35 billion in collateral previously posted by AIG. The result was that counterparties essentially received "par," with Maiden Lane III obtaining the CDOs and AIG obtaining the tear-up of the CDSs.

AIG's $5 billion equity investment in Maiden Lane III was subordinated to the Fed's $24.3 billion secured loan, and the Fed also obtained two-thirds of the upside in Maiden Lane III – securing both downside protection and upside participation for the U.S. taxpayer. Moreover, because Maiden Lane III can hold the underlying CDOs to maturity, it is largely immune from trading prices and liquidity needs, and is therefore in a better position to maximize the value of the CDO portfolio.

The Federal Reserve executed a transaction that involved an asset purchase and the termination of AIG's CDS contracts. By terminating the CDS contracts, the Federal Reserve stopped the collateral calls and the resulting liquidity drain on AIG. By stopping this liquidity drain, the Federal Reserve avoided AIG's downgrade and downward spiral and the resulting threat to the U.S. economy.

IV. Negotiating Concessions from AIG's Counterparties

The Federal Reserve has been criticized by some for not using its regulatory power to force the counterparties to accept less money for the CDOs. The critics overlook a number of key factors.

First, there was little time, and substantial execution risk and attendant harm of not getting the deal done by the deadline of November 10th. As noted above, AIG had attempted for some time to negotiate tear-ups of its CDS contracts with its counterparties under terms more favorable than Maiden Lane III. It did not succeed. When the Federal Reserve reached out to AIG's counterparties, we believed, based on AIG's own experience, that our probability of success of getting them timely to agree to concessions was slim. Even in a best-case scenario, we did not expect that the counterparties would offer anything more than a modest discount to par. In our judgment, taking additional time to press further for a discount was not justified in light of the overwhelming risk and catastrophic consequences of failing to complete the transaction by November 10. Today, it might be tempting to suggest that a transaction that was in the best interests of the taxpayers could have been improved had the New York Fed pressed harder for concessions. But it is much more likely that continuing to push the counterparties toward concessions would not have gotten us to final agreements on November 10th. The consequences to AIG and our economy of failing to reach an agreement made obtaining concessions a lower priority than executing the transactions.

Second, the Federal Reserve had little or no bargaining power given the circumstances. This restructuring negotiation was taking place in November of 2008, less than two months after the decision to rescue AIG from insolvency and the infusion of tens of billions of dollars. The Federal Reserve had already acted to rescue AIG, and the counterparties fully expected that we would stand by that decision, especially because the economic situation had gotten worse, not better. So, the typical threat in such negotiations – we will stand down and watch AIG file for bankruptcy – would have been an idle threat had we made it. In addition, the counterparties were unwilling to offer concessions because their contractual rights were already well-protected. The value of the CDOs they held, combined with the $35 billion of collateral they had previously obtained from AIG was, in most cases, equal to or in excess of par value. Thus, if AIG defaulted, and even filed for bankruptcy protection, the counterparties would have kept both the collateral and the underlying CDOs (and would have been made whole if they had sold the CDOs for fair value).

Finally, even if we had had bargaining power, the rating agencies, as discussed above, were closely examining AIG for signs that it would not be able to address its financial situation. If they saw the Federal Reserve take any action that seemed to suggest a lack of full support, in particular a bankruptcy threat, it might well have led to an immediate downgrade and the irreversible destruction of AIG, with the attendant consequences on the financial stability of our economy.

Some have said that, in the absence of other bargaining power, the Federal Reserve should have used its regulatory power – threatening an adverse use of that power, or suggesting some kind of a benefit flowing from it – to make regulated counterparties give up or compromise their contractual rights. We see that as an abuse of regulatory power. The idea that the Federal Reserve would threaten a financial institution with supervisory action when no grounds for such action exist, or give a financial institution special treatment simply to gain an advantage in a commercial transaction is, in our view, an abuse of our authority. Such conduct by the Federal Reserve might have generated bargaining power over the counterparties, but it is simply inconsistent with the rule of law.

It also would have resulted in unfair treatment of supervised firms. Institutions regulated by the Federal Reserve would have been required to make concessions, while those not subject to the Federal Reserve's supervisory authority would not. As a result, domestic banking organizations regulated by the Federal Reserve would have received less for their property than would foreign banks. This would violate the principle of equality of treatment, a fundamental value of the Federal Reserve.

By getting the eight largest counterparties and AIG to execute term sheets by November 10th, and another eight to do the same shortly thereafter, the Federal Reserve accomplished its overarching goal of avoiding the failure of AIG. As a subsidiary objective, the taxpayers have a well-structured vehicle with downside protection and upside potential, which owns a securities portfolio worth billions more than the loan balance. Moreover, it bears mention that more than $6 billion of the loan has already been repaid.

The situation faced by AIG and the Federal Reserve in the fall of 2008 with respect to the CDS contracts pointedly demonstrates the urgent need for adoption of new resolution procedures for systemically important nonbank financial firms. Had such a tool been available at that time, it could have been used to put AIG into conservatorship or receivership. Not only would this option have allowed AIG to be unwound in an orderly way, protecting policyholders, customers, and taxpayers, but it would have provided a clear and effective mechanism for imposing appropriate haircuts on creditors and counterparties.

AIG's Securities Disclosures

On November 25, 2008, Maiden Lane III began purchasing the underlying CDOs from AIG FP's counterparties. Under SEC rules, because AIG had entered into a "Material Definitive Agreement," it was required to file a Form 8-K with the SEC within four business days. On November 24th, a lawyer for AIG sent a draft version of the 8-K to lawyers for the New York Fed to review, asking for their comments. This made sense: Maiden Lane III was created, funded, and majority-owned by the New York Fed, and AIG wanted to ensure that its public filings would be accurate.

It is commonplace for a publicly traded company to share draft securities filings with another company where the subject matter involves a material transaction affecting both companies. Both the reporting company and the second company – whether the second company is publicly traded or not – want to ensure that the public filing is accurate. What is described here is the kind of thing that routinely happens in major transactions.

Although AIG was consulting regularly with the New York Fed, it is important to note that AIG fully understood that it was wholly responsible for the content of its SEC filings. Indeed, lawyers for both sides were very aware of their respective roles. Lawyers for the New York Fed, both at the Bank and through its outside law firm of Davis Polk & Wardwell LLP, made suggestions about content and timing. AIG and its outside counsel at Sullivan & Cromwell LLP and Weil Gotshal & Manges LLP, accepted the edits that they felt improved the accuracy of the descriptions of the transactions, and declined those edits that they felt did not.

The first 8-K was filed by AIG on December 2, 2008, after Maiden Lane III purchased the first group of CDOs. On December 18 and 22, 2008, Maiden Lane III purchased a second group of CDOs. Also, an agreement struck in November in conjunction with the original transaction, known as the Shortfall Agreement between Maiden Lane III and AIG FP, was amended as of December 18th. These events required the filing of a second 8-K on December 24, 2008. As with the initial public disclosure three weeks earlier, there were many e-mails among all the lawyers before the filing on the 24th. Once again, the New York Fed lawyers had two goals: (1) to help AIG make this filing accurate and consistent with the first; and (2) to protect, where appropriate, the substantial taxpayer funds at stake in Maiden Lane III. And once again, after receiving the New York Fed's suggestions, AIG, aided by its two outside law firms, made the disclosures that they deemed to be legally required and otherwise appropriate.

With that factual backdrop in place, I would now like to turn to the assertions that the New York Fed somehow pressured AIG into "covering up" parts of the transactions in its securities disclosures. There have been four separate allegations, and I would like to address each one in turn.

1. Disclosure of Par Value Payments to CDS Counterparties

First, let me address the assertion that the New York Fed pressured AIG to remove a line in the second 8-K filed on December 24th stating that "the AIG FP counterparties received 100 percent of the par value of the Multi-Sector CDOs sold." The New York Fed believed that disclosure of the actual arithmetic showing that the counterparties received essentially par value was more accurate and would make the new 8-K consistent with AIG's prior 8-K announcing Maiden Lane III. The draft 8-K listed the par value ($16 billion) as well as the amount paid to the counterparties ($6.7 billion), and the amount of collateral previously paid to the counterparties that AIG was surrendering ($9.2 billion). Adding up the last two numbers (which total $15.9 billion) shows that the counterparties were receiving essentially par (which was listed as $16 billion). Because the sum tendered to the counterparties was slightly less than par, the proposed sentence about it being 100 percent of par value (and which was not in the prior 8-K) was not completely accurate, and it was therefore suggested that it be removed.

This was done to be accurate, not to cover up the fact that the counterparties were essentially receiving par. The New York Fed lawyers were motivated by concern for accuracy and precision in the content of these Form 8-Ks. In fact, the clearest evidence that there was no cover up was that it was widely understood in the market and reported in the press at the time that the counterparties were receiving very close to par value. For example, an analyst report published by Credit Suisse on December 2, 2008 – the same day as the initial 8-K filing addressing the first settlements with the counterparties –

opens with the following sentence: "This evening AIG terminated $46.1b of its $71.6b of targeted multi-sector CDO exposure, at par." Similarly, a Fox-Pitt-Kelton report dated the next day, December 3, 2008, contains the following statement: "Along with surrendering $25.9 billion of collateral that had been previously posted by AIG with the counterparties, the purchase of the $46.1 billion of par value essentially made the counterparties whole." On November 12, 2008, a month earlier and shortly after the initial announcement of the Maiden Lane III facility, an article in The Wall Street Journal stated: "The banks that participate will be compensated for the securities' full, or par, value in exchange for allowing AIG to unwind the credit default swaps it wrote." On December 25, 2008, the day after the second 8-K was filed, an article in The Washington Post further reported that, "The fund, called Maiden Lane III, paid about $6.7 billion to the investors for the securities in the latest purchases. The counterparties were also able to keep more than $9 billion that AIG had posted in collateral, reimbursing them at face value for the assets." The fact that the disclosure included all of the actual numbers, and that analysts and the media understood them immediately, belie any assertions of a cover up.

II. Disclosure of Transactions Involving Synthetic CDOs

The second assertion relates to the New York Fed's suggestion to delete that portion of AIG's draft press release accompanying the December 24th 8-K that implied that the New York Fed would enter into additional transactions with AIG concerning the termination of a portfolio of CDS relating to synthetic CDOs. This edit was proposed because there was in fact no commitment at the time for either the Federal Reserve or Maiden Lane III to acquire the synthetic CDOs that backed this portfolio of CDSs.

Indeed, neither the Federal Reserve nor Maiden Lane III has acquired any synthetic CDOs from any counterparty of AIG FP. Thus, rather than seeking to conceal information, the New York Fed comment was made in an effort to help ensure the accuracy of the disclosures so as to avoid any suggestion that the New York Fed had made a commitment that was not made at the time (and in fact was never made). The comment also ensured that there would be no incorrect expectation created in the public markets that such additional Federal Reserve assistance to AIG would be forthcoming.

III. Disclosure of the CDS Counterparties

Third, some have suggested that in November 2008, AIG had planned to disclose the identities of the CDS counterparties and that the New York Fed pressured or compelled AIG not to. This is not true. In December 2008, circumstances were very different than today. Markets were much more fragile, and AIG was concerned at the time that its counterparties, and potentially other AIG customers, would stop doing business with AIG if they believed that the government would cause the disclosure of what is ordinarily confidential customer information, including, in some cases, customer identities. If counterparties and customers began moving away from AIG, the company feared that it would be subject to a loss of business and possible additional downgrades from the rating agencies. This would have had the effect of harming the taxpayers' investment in AIG by reducing the public's interest in doing business with AIG.

For this reason, the New York Fed actively supported AIG's application to the SEC to have the names of its counterparties remain confidential. In March 2009, in response to requests by Congress that the identities of the CDS counterparties be made public, and after taking account of its decision to wind down the AIG FP derivatives business, AIG changed its view and decided to reveal the counterparty names. The Federal Reserve agreed with this decision. Indeed, the counterparty names were disclosed nearly one year ago.

IV. Disclosure of Information Identifying Specific CDOs in the Portfolio

Finally, there have been allegations that the New York Fed inappropriately pressured AIG not to disclose certain commercially sensitive information, including CUSIPs and tranches, that would have identified the individual securities in the Maiden Lane III portfolio. To be sure, the New York Fed actively supported the idea of keeping this information confidential, but once again, only to maximize the value of the Maiden Lane III portfolio for the benefit of the taxpayer.

The portfolio of securities held by Maiden Lane III represents substantial value to the American taxpayer. At the end of the third quarter of 2009, the fair market value of the securities was several billion dollars more than the outstanding balance on the loan. The New York Fed also owns two-thirds of any eventual upside. The New York Fed's investment staff, with the concurrence of its outside advisors, was (and is) strongly of the view that if information identifying these individual securities in the portfolio and the individual prices paid by Maiden Lane III were to become available to traders in such securities, those traders would be able to use that information to their advantage. This, in turn, would undercut the ability of Maiden Lane III to sell those assets for their highest value, to the detriment of taxpayers. Furthermore, as AIG stated in its application to the SEC for confidential treatment, this data does not provide any additional information that would be material to investors in AIG. After lengthy and detailed dialogue, on May 22, 2009, the SEC concluded that this commercially sensitive information need not be disclosed. To be clear, it is only this sensitive security-by-security information that has received confidential treatment and has not been included in AIG's 8-K filings.

The Federal Reserve System shares this committee's goals of transparency and accountability. That is why the Federal Reserve provides weekly public reports on the *aggregate* performance of the Maiden Lane III assets – information that is highly relevant to taxpayers' evaluation of the success of this program, but that does not undercut the ultimate taxpayer recovery that is such an important objective. Also, on a monthly basis, the Federal Reserve publishes a transparency report called "Credit and Liquidity Programs and the Balance Sheet" that provides still more information and analysis regarding Maiden Lane III and the Federal Reserve's other lending programs. This represents a middle ground where our performance as stewards of taxpayer funds can be analyzed and evaluated, but without potentially compromising the taxpayers' prospective return on their investment.

Thank you again for giving me the opportunity to appear before you today. I look forward to answering your questions.

Ms. NORTON. Thank you, Mr. Baxter.

Mr. Habayeb, we are ready for your testimony.

STATEMENT OF ELIAS HABAYEB

Mr. HABAYEB. Madam Chairman, Ranking Member Issa, Members of the committee, thank you for the invitation to appear before you today.

From September 2005 until May of last year, I was senior vice president and chief financial officer of the Financial Services Division at American International Group. I left AIG in May 2009 on excellent terms and continue to provide advisory services to the company while I plan the next phase of my career.

By way of additional background, I am a licensed CPA and practiced with Deloitte and Touche, becoming a partner in 2003.

My position with AIG gave me some insights into Maiden Lane III. Maiden Lane III, LLC, is a financing entity created by the Federal Reserve Bank of New York. The entity helped facilitate the unwinding of a significant portion of AIG financial products' credit default swaps by purchasing the underlying multi-sector CDO bonds from F.P. swap counterparties. At the same time, the related swaps were terminated.

I understand that the committee is interested in learning more about these transactions. These transactions were critical to AIG. They significantly reduced the risk of substantial collateral postings to counterparties that F.P. was required to make under the swaps. They also reduced the erosion to AIG's capital from mounting mark-to-market losses on the swaps.

A little history is helpful. During the subprime mortgage crisis, the bonds underlying F.P. swaps began to decrease in value. As a result, beginning in late 2007 through 2008, F.P. reported billions of dollars of mark-to-market losses on the swaps under the fair value accounting rules. F.P. also posted billions of dollars in collateral to its swap counterparties as a result of the declining market value of the bonds and declines in AIG's and the referenced bonds' credit ratings.

AIG lacked the financial resources to come up with a large-scale solution. Because AIG is not a bank, it did not have access to funding through the Federal Reserve in the normal course. Instead, AIG had to rely on the capital markets.

By the beginning of September 2008, the collateral postings and the mark-to-market losses, along with other factors, were straining AIG's liquidity, but AIG was not able to access the capital markets. On September 15, 2008, the rating agencies downgraded AIG, triggering an onslaught of new collateral calls.

Even after the Federal rescue on September 16, 2008, AIG still needed to reduce its exposure to the mark-to-market losses and collateral calls on F.P. swaps. The Federal rescue did not stop these losses or payment obligations. This is what led to the creation of Maiden Lane III.

Under the terms negotiated by the New York Fed with the swap counterparties, Maiden Lane III bought the underlying bonds at the then-market value. Specifically, Maiden Lane III purchased approximately $62 billion notional amount of bonds underlying F.P. swaps for a market value of $29 billion. Separately, F.P. agreed to terminate the swaps for an amount equal to the difference of the bonds' notional par value and its market value. The collateral that F.P. had posted to date was used to pay the cost of terminating the swaps. Specifically, F.P. paid the counterparties approximately $33 billion in previously-posted collateral to tear up the swaps. So the counterparties ended up with par, a total of approximately $62 billion.

To conclude, Maiden Lane III was critical in mitigating AIG's continued exposure to the significant mark-to-market losses and collateral calls on the swaps that was draining AIG's capital and liquidity.

I am happy to answer any questions the Members of the committee may have.

Thank you.

[The prepared statement of Mr. Habayeb follows:]

TESTIMONY OF ELIAS HABAYEB

BEFORE THE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

UNITED STATES HOUSE OF REPRESENTATIVES

JANUARY 27, 2010

MR. CHAIRMAN, RANKING MEMBER ISSA, MEMBERS OF THE COMMITTEE. THANK YOU FOR THE INVITATION TO APPEAR BEFORE YOU TODAY.

FROM SEPTEMBER 2005 UNTIL MAY OF LAST YEAR, I WAS SENIOR VICE PRESIDENT AND CHIEF FINANCIAL OFFICER OF THE FINANCIAL SERVICES DIVISION OF AMERICAN INTERNATIONAL GROUP, INC. AIG'S SUBSIDIARIES WITHIN THE FINANCIAL SERVICES DIVISION ENGAGE IN A DIVERSE RANGE OF ACTIVITIES INCLUDING AIRCRAFT AND EQUIPMENT LEASING, CAPITAL MARKETS, CONSUMER FINANCE AND INSURANCE PREMIUM FINANCE. THESE SUBSIDIARIES INCLUDE AIG FINANCIAL PRODUCTS CORP. ("FP"). AS HAS BEEN WIDELY REPORTED, FP IS THE UNIT THAT WROTE THE CREDIT DEFAULT SWAPS (THE "SWAPS") PROTECTING MULTI-SECTOR COLLATERALIZED DEBT OBLIGATIONS (THE "BONDS") THAT HAD EXPOSURE TO THE U.S. SUBPRIME MORTGAGE MARKET AND THAT CONTRIBUTED GREATLY TO AIG'S LIQUIDITY CRISIS IN SEPTEMBER 2008.

BY WAY OF BACKGROUND, I AM A LICENSED CPA AND I PRACTICED WITH DELOITTE & TOUCHE LLP, BECOMING A PARTNER IN 2003, BEFORE I WAS RECRUITED TO AIG IN 2005. I LEFT EMPLOYMENT WITH AIG IN MAY 2009 ON EXCELLENT TERMS, AND CONTINUE TO PROVIDE ADVISORY SERVICES TO THE COMPANY WHILE I PLAN THE NEXT PHASE OF MY CAREER.

MY POSITION WHILE I WAS EMPLOYED BY AIG GAVE ME SOME INSIGHT INTO THE CREATION OF WHAT IS COMMONLY REFERRED TO AS "MAIDEN LANE III". MAIDEN LANE III LLC IS A FINANCING VEHICLE CREATED BY THE NEW YORK FEDERAL RESERVE BANK ("NY FED") THAT HELPED FACILITATE THE UNWINDING OF A SIGNIFICANT PORTION OF FP'S SWAPS BY PURCHASING THE UNDERLYING BONDS FROM FP'S SWAP COUNTERPARTIES. AT THE SAME TIME, THE RELATED SWAPS WERE TERMINATED.

I ALSO WAS INVOLVED IN AIG'S EARLY AND UNSUCCESSFUL EFFORTS TO REDUCE FP'S RISK EXPOSURE, INCLUDING BY TERMINATING FP'S SWAPS. ULTIMATELY, THE NEW YORK FED TOOK CONTROL OF THE NEGOTIATIONS WITH FP'S COUNTERPARTIES TO THE SWAPS. THE NEW YORK FED COMPLETED THAT PROCESS THROUGH MAIDEN LANE III. AFTER THE TRANSACTIONS WERE COMPLETED, I, ALONG WITH OTHERS, REVIEWED AIG'S FILINGS WITH THE SECURITIES AND EXCHANGE COMMISSION TO HELP ENSURE THAT THEY ACCURATELY DESCRIBED THESE TRANSACTIONS.

I UNDERSTAND THAT THE COMMITTEE IS INTERESTED IN LEARNING MORE ABOUT THE MAIDEN LANE III TRANSACTIONS. THESE TRANSACTIONS WERE CRITICAL TO AIG IN ORDER TO MATERIALLY REDUCE THE RISK OF SUBSTANTIAL COLLATERAL POSTINGS TO COUNTERPARTIES THAT FP WAS REQUIRED TO MAKE UNDER THE SWAPS AND ALSO TO REDUCE THE EROSION TO AIG'S CAPITAL FROM MOUNTING MARK-TO-MARKET LOSSES ON THE SWAPS.

I PAUSE FOR A MOMENT TO RECOUNT SOME CONTEXT BECAUSE I BELIEVE IT SHEDS LIGHT ON WHY MAIDEN LANE III WAS NECESSARY.

FIRST, IT IS IMPORTANT TO UNDERSTAND THE NATURE OF AIG'S EXPOSURE TO THE SWAPS BECAUSE AIG GUARANTEED FP'S DEBT OBLIGATIONS SINCE FP'S INCEPTION IN 1987.

SINCE 1998, FP WROTE SWAPS THAT PROVIDED CREDIT PROTECTION ON MULTI-SECTOR COLLATERALIZED DEBT OBLIGATIONS (REFERRED TO HERE AS THE BONDS). AS OF SEPTEMBER 30, 2008, THE TOTAL NOTIONAL VALUE OF THE BONDS WAS APPROXIMATELY $72 BILLION.

FP'S COUNTERPARTIES TO THESE SWAPS WERE MOSTLY LARGE US AND INTERNATIONAL FINANCIAL INSTITUTIONS. THE COUNTERPARTIES PURCHASING THE SWAPS PAID FP PERIODIC PREMIUMS IN EXCHANGE FOR FP ASSUMING THE RISK THAT THE COUNTERPARTIES HAD OF NON-PAYMENT OR

LOSS RESULTING FROM CERTAIN "CREDIT EVENTS" (*E.G.*, FAILURE TO PAY, BANKRUPTCY, ACCELERATION, RESTRUCTURING) WITH RESPECT TO THE UNDERLYING BONDS.

FP WAS ALSO REQUIRED UNDER CERTAIN CIRCUMSTANCES TO POST COLLATERAL TO THE COUNTERPARTIES – SECURING FP'S ABILITY TO PERFORM IN THE EVENT OF A DEFAULT OR OTHER CREDIT EVENT TRIGGERING A PAYMENT OBLIGATION ON THE SWAP.

GENERALLY, THE AMOUNT OF COLLATERAL REQUIRED TO BE POSTED BY FP UNDER THE SWAPS WAS DETERMINED BY A FORMULA THAT TOOK INTO ACCOUNT AIG'S CREDIT RATINGS, THE UNDERLYING BOND'S CREDIT RATINGS, AND THE MARKET VALUE OF THE UNDERLYING BOND. TO SIMPLIFY, IF THE VALUE OF THE BONDS COVERED BY THE SWAP, THE UNDERLYING BOND'S CREDIT RATING, OR AIG'S CREDIT RATING DROPPED, FP HAD TO POST COLLATERAL "FOR THE PROTECTION" OF ITS COUNTERPARTY.

DURING THE SUB-PRIME MORTGAGE CRISIS, THE BONDS UNDERLYING FP'S SWAPS BEGAN TO DECREASE IN VALUE. AS A RESULT, BEGINNING IN LATE 2007 THROUGH 2008, FP REPORTED BILLIONS OF DOLLARS OF MARK-TO-MARKET LOSSES ON THE SWAPS UNDER THE FAIR VALUE ACCOUNTING RULES. (AS CFO OF THE FINANCIAL SERVICES DIVISION, I WAS INVOLVED IN ACCOUNTING FOR THE SWAPS, EVEN THOUGH I WAS NOT INVOLVED IN WRITING THE SWAPS –

INDEED, THE MAJORITY OF THE SWAPS WERE ON FP'S BOOKS BEFORE I JOINED AIG.) THESE VALUATION LOSSES COULD (AND INITIALLY WERE EXPECTED TO) REVERSE IF THE FAIR VALUE OF THE SWAPS RECOVERED AND FP STILL HELD THE SWAPS.

FP ALSO POSTED BILLIONS OF DOLLARS IN COLLATERAL TO ITS COUNTERPARTIES UNDER THE SWAPS AS A RESULT OF THE DECLINING MARKET VALUE OF THE BONDS AND DECLINES IN AIG AND THE BONDS' CREDIT RATINGS.

IN LIGHT OF THESE MOUNTING LOSSES, BEGINNING IN THE SUMMER OF 2008, BEFORE THE FEDERAL RESCUE, I WAS ACTIVELY INVOLVED, ALONG WITH OTHERS AT AIG AND ITS ADVISORS, IN EXPLORING POSSIBILITIES TO REDUCE THE LIQUIDITY AND MARK-TO-MARKET RISKS POSED BY FP'S SWAPS.

HOWEVER, AIG LACKED THE FINANCIAL RESOURCES TO COME UP WITH A LARGE SCALE SOLUTION INVOLVING A $72 BILLION BOOK OF SWAPS. EVEN THOUGH AIG HAD MANY ASSETS, MOST WERE ASSETS HELD BY ITS INSURANCE COMPANY SUBSIDIARIES, AND STATE INSURANCE REGULATIONS SEVERELY LIMITED AIG'S ABILITY TO ACCESS THEM. BECAUSE AIG IS NOT A BANK, IT DID NOT HAVE ACCESS TO FUNDING THROUGH THE FEDERAL RESERVE IN THE NORMAL COURSE. INSTEAD, AIG HAD TO RELY ON THE CAPITAL MARKETS. BUT AIG WAS UNABLE TO OBTAIN ADDITIONAL LIQUIDITY FROM THE CAPITAL MARKETS.

ADDITIONALLY, OUR EFFORTS TO STEM THE TIDE OF COLLATERAL CALLS AND REDUCE FP'S RISK EXPOSURE BY NEGOTIATING WITH COUNTERPARTIES DURING THIS PERIOD WERE UNSUCCESSFUL. UNFORTUNATELY, WE HAD LITTLE NEGOTIATING LEVERAGE WITH FP'S COUNTERPARTIES TO EXTRACT DISCOUNTS. THE CONTRACTUAL COLLATERAL POSTING PROVISIONS IN THE SWAPS WERE A SOURCE OF CHEAP CASH FOR THEM. IT WAS ALSO MY UNDERSTANDING THAT EVEN IF FP OR AIG FILED FOR BANKRUPTCY, THE COUNTERPARTIES WOULD KEEP THE COLLATERAL FP HAD POSTED TO DATE, THEY WOULD KEEP THE UNDERLYING BONDS (AND ANY FUTURE UPSIDE), AND THEY COULD MAKE A CLAIM AGAINST FP FOR DEFAULTING ON THE SWAPS.

BY AUGUST 31, 2008, FP HAD POSTED $19 BILLION IN COLLATERAL TO FP'S SWAP COUNTERPARTIES. AND BY THE BEGINNING OF SEPTEMBER 2008, FP'S COLLATERAL PAYMENT OBLIGATIONS (AS WELL AS CASH REQUIREMENTS IN CERTAIN OF AIG'S OTHER BUSINESS SEGMENTS) WERE PLACING INCREASING STRESS ON AIG'S LIQUIDITY. ON SEPTEMBER 15, 2008, THE RATING AGENCIES DOWNGRADED AIG'S CREDIT RATING, TRIGGERING AN ONSLAUGHT OF NEW COLLATERAL CALLS.

EVEN AFTER THE FEDERAL RESCUE ON SEPTEMBER 16, 2008, AIG STILL NEEDED TO DO SOMETHING TO REDUCE ITS EXPOSURE TO THE MARK-TO-MARKET LOSSES AND COLLATERAL CALLS ON FP'S SWAPS. THE FEDERAL

RESCUE DID NOT STOP THESE LOSSES OR PAYMENT OBLIGATIONS. INDEED, FP POSTED APPROXIMATELY $12.5 BILLION IN THE MONTH OF SEPTEMBER ALONE. AND AS THE LOSSES AND PAYMENTS CONTINUED, AIG FACED YET ANOTHER RATINGS DOWNGRADE THAT COULD HAVE FURTHER STRAINED AIG'S LIQUIDITY BY TRIGGERING YET MORE COLLATERAL CALLS OR PERMITTING COUNTERPARTIES TO TERMINATE SWAPS AT PRICES FAVORABLE TO THEM.

IN OUR ONGOING DISCUSSIONS WITH COUNTERPARTIES DURING THIS PERIOD, THE COUNTERPARTIES WERE UNWILLING TO ACCEPT LESS THAN PAR VALUE. SOME COUNTERPARTIES WERE WILLING TO TERMINATE THE SWAPS, BUT ONLY IF AIG PURCHASED THE UNDERLYING BONDS FROM THEM – SOMETHING AIG COULD NOT DO WITHOUT THE NY FED'S HELP.

ON SEPTEMBER 30, 2008, I, OTHERS AT AIG, AS WELL AS AIG'S FINANCIAL ADVISORS AND LEGAL COUNSEL, PRESENTED TO THE NY FED AND ITS FINANCIAL ADVISORS, SEVERAL OPTIONS FOR ADDRESSING THE LIQUIDITY AND MARK-TO-MARKET LOSSES. THE OPTIONS AVAILABLE TO AIG WITHOUT NY FED SUPPORT WERE LIMITED GIVEN AIG'S LACK OF FINANCIAL RESOURCES AND ACCESS TO THE CAPITAL MARKET. BUT A LARGE SOLUTION WAS CRITICAL TO REDUCING THE LIKELIHOOD OF A FURTHER DOWNGRADE OF AIG'S RATING.

ONE OF THE OPTIONS PRESENTED WAS FOR FP AND THE NY FED TO CREATE A SPECIAL PURPOSE VEHICLE FUNDED LARGELY BY THE NY FED AND

FP'S EXISTING COLLATERAL POSTINGS THAT WOULD PAY TO ACQUIRE THE UNDERLYING BONDS AND TERMINATE THE RELATED SWAPS. (THIS OPTION WAS VERY SIMILAR TO MAIDEN LANE III.) THIS OPTION WOULD REDUCE FP'S EXPOSURE TO MARK TO MARKET LOSSES AND COLLATERAL CALLS BUT WOULD NECESSITATE A LARGE UPFRONT FUNDING REQUIREMENT.

UNDER THE FINAL MAIDEN LANE III STRUCTURE, THE NY FED WOULD LEND UP TO $30 BILLION AND AIG WOULD PROVIDE $5 BILLION IN EQUITY FUNDING TO MAIDEN LANE III AND MAIDEN LANE III WOULD BUY THE BONDS UNDERLYING THE SWAPS FROM FP'S COUNTERPARTIES. MAIDEN LANE III WOULD COLLECT CASH FLOWS FROM THE BONDS AND PAY A DISTRIBUTION TO AIG FOR ITS EQUITY INTEREST ONCE THE PRINCIPAL AND INTEREST OWING TO THE NY FED ON ITS LOAN HAD BEEN PAID DOWN IN FULL. UPON PAYMENT IN FULL OF THE NY FED'S LOAN AND AIG'S EQUITY INTEREST, ALL REMAINING AMOUNTS RECEIVED BY THE ENTITY WOULD BE PAID 67 PERCENT TO THE NY FED AND 33 PERCENT TO AIG.

THIS ARRANGEMENT ALLOWED BOTH THE NY FED AND AIG TO RETAIN THE UPSIDE FROM THE BONDS – FUTURE CASH FLOWS.

ON OCTOBER 31, 2008, I WAS TOLD THAT THE NY FED AND ITS FINANCIAL AND LEGAL ADVISORS TOOK OVER NEGOTIATIONS WITH THE COUNTERPARTIES AND ALL EFFORTS WERE NOW FOCUSED ON IMPLEMENTING THE MAIDEN LANE

III SOLUTION. I PERIODICALLY RECEIVED UPDATES ABOUT THE NY FED'S PROGRESS IN THESE NEGOTIATIONS.

UNDER THE FINAL TERMS NEGOTIATED BY THE NY FED, MAIDEN LANE III (THE FINANCING ENTITY CREATED BY THE NY FED), BOUGHT THE UNDERLYING BONDS AT THEIR THEN MARKET VALUE – NOT AT PAR. SEPARATELY, FP AGREED TO TERMINATE THE SWAPS FOR AN AMOUNT EQUAL TO THE DIFFERENCE OF THE BONDS' NOTIONAL (PAR) VALUE AND ITS MARKET VALUE. THE COLLATERAL THAT FP HAD POSTED TO DATE WAS USED TO PAY THE COST OF TERMINATING THE SWAPS. SO, THE COUNTERPARTIES ENDED UP WITH PAR.

AS AIG DISCLOSED IN AN SEC FILING ON DECEMBER 2, 2008, MAIDEN LANE III PURCHASED APPROXIMATELY $46.1 BILLION NOTIONAL AMOUNT OF BONDS UNDERLYING FP'S SWAPS AND TERMINATED THE ASSOCIATED SWAPS ON NOVEMBER 25, 2008. THE AGGREGATE COST OF THE PURCHASES AND TERMINATIONS WAS FUNDED THROUGH APPROXIMATELY $15.1 BILLION OF BORROWINGS UNDER THE NY FED LOAN TO MAIDEN LANE III, AIG'S $5 BILLION EQUITY FUNDING AND THE SURRENDER OF APPROXIMATELY $25.9 BILLION OF COLLATERAL PREVIOUSLY POSTED BY FP TO THE SWAP COUNTERPARTIES.

ON DECEMBER 18 AND 22, 2008, MAIDEN LANE III ACQUIRED $16 BILLION IN PAR AMOUNT OF ADDITIONAL BONDS. AS DISCLOSED IN AN SEC FILING ON DECEMBER 24, 2008, THIS PURCHASE WAS FUNDED WITH A NET PAYMENT TO

COUNTERPARTIES OF APPROXIMATELY $6.7 BILLION. ADDITIONALLY, FP SURRENDERED APPROXIMATELY $9.2 BILLION IN COLLATERAL PREVIOUSLY POSTED TO FP'S SWAP COUNTERPARTIES TO TERMINATE THE SWAPS. IN CONNECTION WITH THE TERMINATION OF THE SWAPS, FP GOT BACK $2.5 BILLION IN EXCESS COLLATERAL IT HAD PREVIOUSLY POSTED UNDER THE SWAPS.

IN SUM, MAIDEN LANE III PURCHASED APPROXIMATELY $62 BILLION IN NOTIONAL AMOUNT OF BONDS UNDERLYING FP'S SWAPS FOR A MARKET VALUE OF $29 BILLION. FP PAID THE COUNTERPARTIES IN PREVIOUSLY POSTED COLLATERAL, $33 BILLION, TO TEAR UP THE SWAPS.

I UNDERSTAND THE COMMITTEE IS ALSO INTERESTED IN AIG'S DISCLOSURES ABOUT MAIDEN LANE III. AFTER THE MAIDEN LANE III TRANSACTIONS WERE COMPLETED, I, ALONG WITH OTHERS, REVIEWED AIG'S FILINGS WITH THE SEC TO HELP ENSURE THEIR ACCURACY BECAUSE OF MY FAMILIARITY WITH THE TERMS OF THE MAIDEN LANE III TRANSACTIONS. I DID NOT DECIDE WHAT EXHIBITS OR SCHEDULES WERE DISCLOSED. AIG HAD OUTSIDE LEGAL COUNSEL WHO GUIDED THE COMPANY THROUGH THAT PROCESS.

TO CONCLUDE, MAIDEN LANE III WAS CRITICAL IN HELPING AIG TO ELIMINATE MOST OF ITS CONTINUED EXPOSURE TO THE SIGNIFICANT MARK-TO-

MARKET LOSSES AND COLLATERAL CALLS ON THE SWAPS THAT WERE DRAINING AIG'S LIQUIDITY.

I AM HAPPY TO ANSWER ANY QUESTIONS THE MEMBERS OF THE COMMITTEE MAY HAVE. THANK YOU.

Ms. NORTON. Thank you very much, Mr. Habayeb.

Mr. Friedman.

STATEMENT OF STEPHEN FRIEDMAN

Mr. FRIEDMAN [Remarks off mic]. As indicated in my prepared statement, I have little factual information to offer in response to the questions set forth in the committee's invitation for me to testify. The explanation for my lack of involvement in the New York Reserve Bank AIG counterparty transactions requires an appreciation of the limited role that a Reserve Bank's chairman and Board of Directors play in a Reserve Bank's operation.

A Reserve Bank's Board of Directors is really more akin to an advisory board. It is actually sort of a hybrid, more akin to that than it is to the Board of Directors of a typical corporation. Reserve Bank Directors serve part-time, make observations on the economy and markets, make recommendations on monetary policy, and approve the bank's budget, internal controls and policies and procedures, and personnel matters.

But consistent with the structure created by the Federal Reserve Act, the Directors of the 12 Federal Reserve Banks have no role in the regulation, supervision, or oversight of banks, bank holding companies or other financial institutions. Such responsibilities, including the extraordinary financial interventions of 2008, are instead carried out by the officers of the 12 regional Federal Reserve Banks acting at the direction and with the oversight of the Board of Governors of the Federal Reserve System in Washington. In other words, the Board of Governors in Washington effectively is the Board of Directors for Reserve Bank undertakings such as the AIG financial rescue transactions.

Accordingly, as I explained to committee staff and consistent with the Fed's ground rules, whether as chairman of the New York Federal Reserve Board or otherwise, I was not involved in the decision to bail out AIG, the decision to repay the AIG counterparties at par, or the decision not to publicly disclose those counterparties' names. I did not ratify those decisions and I do not know just who made those decisions.

I am advised that on the evening of November 9, 2008, the Chair of the bank's Audit Committee and I received a telephonic summary briefing from bank officials about the transaction. At that point, the deal had been signed up and was to be announced by the Board of Governors the next morning.

Finally, I would note that by statutory design, the Boards of the Reserve Banks are comprised of members with intentionally diverse financial interests and affiliations, such that the Directors' recommendations and advice on monetary policy include input from a diverse array of bankers, borrowers, and community leaders.

Because the Boards, once again by statutory design, include bank executives and bank shareholders, many current Directors would have conflicts of interest if the Reserve Bank Boards of Directors also had any authority over, or any role in, individual supervisory matters like the New York Reserve Bank's rescue of AIG and the AIG counterparty transactions. But the New York Reserve Board does not have such authority, and it and I were walled off from these matters—really ring-fenced.

I stand ready to answer any questions the committee may have.

[The prepared statement of Mr. Friedman follows:]

As Revised

United States House of Representatives
Committee on Oversight and Government Reform

"Factors Affecting Efforts to Limit Payments to AIG Counterparties"
Prepared Testimony of Stephen Friedman
January 27, 2010

Mr. Chairman, Ranking Member Issa, and Members of the Committee,

I am here today because of my great respect for Congress and the essential role that it plays in the United States Government. It was my recent privilege to serve my country in the Executive Branch as Assistant to the President for Economic Policy and Director of the National Economic Council from 2002 to 2004, and as Chairman of the President's Foreign Intelligence Advisory Board from 2006 to 2009, and I developed a renewed appreciation of our Constitutional system of checks and balances.

Despite my recognition of the importance of the Committee's inquiry, I cannot provide the Committee with any insight into the principal subject of today's hearing—the transaction that paid AIG's credit default swap counterparties at par.

The questions raised about these transactions reflect understandable confusion about the role that a Reserve Bank's Chairman and Board of Directors play in a Reserve Bank's operations. Consistent with the structure created by the Federal Reserve Act, the Board of Directors of the New York Federal Reserve Bank has no role in the regulation, supervision, or oversight of banks, bank holding companies, or other financial institutions. Such responsibilities are instead carried out by the officers of the New York Federal Reserve Bank acting at the direction of the Board of Governors of the Federal Reserve System here in Washington.

A Reserve Bank's Board of Directors in many respects is more akin to an "Advisory Board" than it is to the Board of Directors of a corporation. Reserve Bank Directors "make recommendations on monetary policy," including approving the recommended discount rate subject to Board of Governors approval, and are responsible for approving the Bank's budget, reviewing the Bank's internal controls and policies and procedures, and overseeing personnel matters, including assisting in the selection of the Bank President and other senior Bank officers. But the Board of Directors of a Reserve Bank has no authority over, and is walled-off from, regulatory and supervisory policies and actions involving banks, bank holding companies, and other financial institutions.

Accordingly, as I explained to Committee staff, whether as Chairman of the New York Federal Reserve Board or otherwise, I was not involved in the initial decision to bail out AIG, the decision to repay the AIG counterparties at par, or the decision not to publicly disclose those counterparties' names. I did not ratify those decisions; and I do not know who made those decisions.

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Not only was I not involved in the Reserve Bank's decisions regarding the supervision and management of AIG, but my actual knowledge of those decisions is extraordinarily limited. I did receive summary briefings from senior Reserve Bank officers regarding both the initial September 16, 2008 rescue of AIG and the November 10, 2008 transaction to repay AIG's counterparties at par, although in both instances the briefing occurred after the transactions already had been negotiated. In the case of the November 10 transaction, I have been advised that on the evening of November 9, 2008, Charles Wait—the Chair of the Bank's Audit Committee—and I received a telephonic summary briefing from Bank officials about the transaction. At that point the deal had been signed up and was to be announced by the Board of Governors the next morning. As to the decision not to disclose the names of AIG's counterparties, I do not recall receiving any briefings on that subject.

* * *

The Committee also has inquired about my purchases of Goldman Sachs stock on December 17, 2008 and January 22, 2009, subsequent to the decision to repay AIG's counterparties at par on November 10, 2008.

As is shown in the attached chronology, at the time of my purchases, it was widely known and reported – through various public statements by Goldman Sachs officials, in numerous contemporaneous newspaper articles, in multiple investment analysts' reports, and in the November 10 Federal Reserve Board and AIG press releases – that Goldman Sachs was a counterparty to AIG and had been repaid at par on November 10. Indeed, the December 17, 2008 purchase occurred the day after Goldman Sachs' quarterly earnings release and an earnings call statement by its CFO that its exposure to AIG "has been immaterial" and "is still immaterial."

Consistent with company policy to ensure that statutory "insiders" do not trade in Goldman Sachs securities while in possession of any undisclosed material information, I consulted with and received the approval of the Goldman Sachs General Counsel's office prior to executing the December 17 and January 22 trades, as being within a "window" during which Goldman Sachs Directors were permitted to trade. These purchases promptly were publicly disclosed in filings with the Securities and Exchange Commission.

In addition, my purchases, in the words of the General Counsel of the New York Reserve Bank, "did not violate any Federal Reserve statute, rule or policy." When I was appointed in January 2008 to the New York Reserve Board of Directors as Chairman and as a Class C Director, the New York Reserve Bank and the Board of the Governors of the Federal Reserve System were aware that I was a Director of Goldman Sachs, that I held a significant amount of Goldman Sachs stock, and that I was scheduled annually to receive additional Goldman Sachs restricted stock by virtue of my service as a Goldman Sachs Director. When Goldman Sachs became a bank holding company on September 21, 2008, I became technically ineligible to serve as Class C Director because Class C Directors cannot own bank holding company stock (Class A and Class B Directors can own bank holding company stock) and because Class C Directors cannot serve as officers or directors of banks (Class A Directors can serve as officers and directors of banks). At that point, the Board of Governors either could request my resignation as a Class C Director, or, as subsequently occurred, could "waive" the eligibility requirements with respect to my ownership of Goldman Sachs stock and service on the Goldman Sachs Board.

At the time of my selection and appointment as Reserve Board Chairman, I had been forewarned that I would be expected to spend considerable time leading the search for Mr. Geithner's replacement as President of the New York Reserve Bank in the event he accepted another position. I therefore was not surprised that, a month before the November 2008 election and at a time of great stress in the financial markets, the New York Reserve Bank requested such a waiver, following consultation with the Board of Governors staff. I thereafter continued to serve as Board Chairman and a Director, with the understanding that I was permitted to do so by Federal Reserve policies and precedents until the expected waiver was granted.

Immediately upon Mr. Geithner's selection by President-elect Obama as Secretary of the Treasury-Designate on November 24, 2008, the New York Reserve Bank Board, under my leadership, commenced a thorough and expedited search process for his replacement, in close coordination with the Board of Governors, which concluded in late January 2009. In early December, I inquired about the status of the Bank's waiver request, and, as has been publicly reported, I was informed by the General Counsel of the New York Reserve Bank that I should consider the eligibility requirements to be in abeyance while the request for a waiver was pending. The waiver was issued on January 21, 2009, without any conditions upon my increasing my ownership of Goldman Sachs stock.

I am advised that the Board of Governors three months ago published a new policy regarding the eligibility, qualifications, and rotation of Reserve Bank Directors, which expressly addresses the situation I faced and now provides a 60-day period for resolving (whether through waiver, divestiture, or resignation) a situation where a Director becomes ineligible to serve because of a change in the status of a financial institution. I note that if this policy had been in place in September 2008, it would have abbreviated the delay that occurred in the processing of the Reserve Bank's waiver request on my behalf.

When I was appointed by the President of the United States as Director of the National Economic Council in 2002, I divested all of my ownership interests in individual companies and entities, including my Goldman Sachs holdings, to avoid any possibility of a potential conflict of interest. I approached my appointment as Director and Board Chairman of the New York Federal Reserve Bank with the same public service mindset. By statutory design, the Reserve Bank Board is comprised of Members with intentionally diverse financial interests and affiliations that theoretically would present potential conflicts of interest, if the Board of Directors had any authority over or role in individual supervisory matters – matters like the New York Reserve Bank's rescue of AIG. But the Board does not have such authority and it did not play such a role.

As Revised

I stand ready to answer any questions that the Committee may have.

Attachment – Chronology of Selected Events and Disclosures

As Revised

Chronology of Selected Events and Disclosures

Attachment to the Prepared Testimony of Stephen Friedman
January 27, 2010

Jan. 1, 2008	Mr. Friedman appointed Chairman and "Class C Director" of New York Fed by the Board of Governors of the Federal Reserve; at the time of his appointment, the Board of Governors is made aware of Mr. Friedman's financial interests in Goldman Sachs (including expected annual awards of restricted stock) and his position as Director of The Goldman Sachs Group.
Sept. 16, 2008	The Federal Reserve Board (through the New York Fed) pledges $85 billion to AIG. FRB Press Release, *Federal Reserve Board, with full support of the Treasury Department, authorizes the Federal Reserve Bank of New York to lend up to $85 billion to the American International Group (AIG)*, Sept. 16, 2008, *available at* http://www.federalreserve.gov/newsevents/press/other/20080916a.htm.
Sept. 16, 2008	In response to a question about Goldman Sachs' exposure to AIG, Goldman Sachs CFO David A. Viniar tells investors: "The way we do business with financial institutions is by having appropriate daily margin terms. ... That is how we manage our risk. In addition to the margin terms, we augment our risk management with appropriate hedging strategies. ... [W]hatever the outcome at AIG, I would expect the direct impact of our credit exposure to both of them to be immaterial to our results." Goldman Sachs Q3 2008 Earnings Call.
Sept. 16, 2008	A Bank of America equity research report notes: "While both LEH & AIG are large, important counterparties to GS, mgmt expects the direct impact of outcomes at both firms to be immaterial to results given hedging strategies and the firm's commitment to avoiding large concentrated positions." Michael Hecht, *The Goldman Sachs Group, Inc.: You Can Run But You Can't Hide; No Immunity from Cyclical Challenges*, Bank of America Equity Research (Sept. 16, 2008).
Sept. 17, 2008	Sandler O'Neill & Partners reports that "A point of management emphasis was on the firm's desire to avoid large concentrated exposures. To this effect, management successfully mitigated its risk to LEH and AIG. While both important counterparties, conservative daily margin terms reduced the risk of doing business with these institutions as well as other counterparties. With that said, management expects that the direct impact of GS's credit exposure to these firms will be 'immaterial' to results." *Goldman Sachs Group, Inc.: 3Q08 Earnings Review*, Sandler O'Neill & Partners, L.P. (Sept. 17, 2008).
Sept. 17, 2008	William Blair reports: "Lehman Holdings (LEH $0.30) and AIG (AIG $3.75) are certainly both important counterparties to Goldman Sachs; although Goldman has worked hard to avoid large direct exposures to any single counterparty by managing margin terms and hedging strategies. Management commented that Goldman Sachs' 'direct' impact to the unwinding of both Lehman and AIG would not be material. The Fed-led bailout of AIG certainly reduces any potential strain from any credit exposure to the company or exposure to others that may have outsized exposures to AIG." Mark Lane and Katherine McCauley, *The Goldman Sachs Group, Inc.: Highlights of Fiscal Third-Quarter Results; No Surprises in The Face of Subdued Expectations in Very Challenging Environment*, William Blair & Company, L.L.C. (Sept. 17, 2008).
Sept. 21, 2008	Board of Governors of the Federal Reserve approves applications of The Goldman Sachs Group, Inc. and Goldman Sachs Bank USA Holdings LLC to convert to bank holding companies. Goldman Sachs Press Release, *Goldman Sachs To Become The Fourth Largest Bank Holding Company*, Sept. 21, 2008, *available at* http://www2.goldmansachs.com/our-firm/press/press-releases/archived/2008/bank-holding-co.html.

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Chronology of Selected Events and Disclosures

Sept. 23, 2008	Berkshire Hathaway agrees to purchase $5 billion in Goldman's preferred stock, and also received warrants to buy another $5 billion in Goldman's common stock, exercisable for a five-year term. Susanne Craig, Matthew Karnitschnig and Aaron Lucchetti, *Buffett to Invest $5 Billion in Goldman*, WALL STREET JOURNAL, Sept. 24, 2008.
Sept. 24, 2008	Goldman Sachs announces a public offering of $5 billion in common shares. Goldman Sachs Press Release, *Goldman Sachs Prices $5 Billion Public Offering of Common Equity*, Sept. 24, 2008.
Sept. 28, 2008	The NY Times reports that "Goldman Sachs was a member of A.I.G.'s derivatives club ... It was a customer of A.I.G.'s credit insurance and also acted as an intermediary for trades between A.I.G. and its other clients." The article further reports that Goldman Sachs had $20 billion of transactions with AIG, and also includes statements from several Goldman Sachs executives that its exposure to AIG was "immaterial" because of hedges. Gretchen Morgenson, *Behind Insurer's Crisis, Blind Eye to a Web of Risk*, NY TIMES, Sept. 28, 2008.
Sept. 28, 2008	Reuters reports that Goldman was AIG's "largest trading partner" and had $20 billion of transactions with AIG, but disputes Goldman's level of exposure. Lucas van Praag, a Goldman Sachs spokesman, is quoted in the article, noting that: "we have said many times on the record that our exposure to AIG was, and is, not material ... For the avoidance of doubt, our exposure to AIG is offset by collateral and hedges and is not material to Goldman Sachs in any way." *Goldman Sachs faults NY Times story on AIG risk*, REUTERS, Sept. 28, 2008.
Sept. 29, 2008	Goldman Sachs completes its public offering, which is oversubscribed. Total proceeds are $5.75 billion. Goldman Sachs 2008 Fourth Quarter Earnings Report, *available at* http://www2.goldmansachs.com/our-firm/press/press-releases/archived/2008/pdfs/2008-q4-earnings.pdf; *See also Goldman Sachs raises $5b with public stock offering*, AP, Sept. 25, 2008.
Oct. 6, 2008	New York Fed (via letter from Timothy Geithner) seeks waiver of Fed rules against board members owning stock or being a director of bank holding companies; letter specifies that Mr. Friedman is a Director of and holds financial interests in The Goldman Sachs Group.
Oct. 8, 2008	The Federal Reserve Board (through the New York Fed) pledges an additional $37.8 billion to AIG. FRB Press Release, *Board authorizes Federal Reserve Bank of New York to borrow securities from certain regulated U.S. insurance subsidiaries of AIG*, Oct 8, 2008, *available at* http://www.federalreserve.gov/newsevents/press/other/20081008a.htm.

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Chronology of Selected Events and Disclosures

Oct. 31, 2008	The Wall Street Journal reports that AIG has posted "about $50 billion in collateral to its trading partners" and that these payments "have continued to balloon after the bailout." The story notes that "Goldman Sachs Group Inc., for instance, has pried from AIG $8 billion to $9 billion, covering virtually all its exposure to AIG – most of it before the U.S. stepped in." The Journal reported further that Goldman had become concerned about exposure to AIG in 2007 and had hedged its exposure: AIG's trading partners were worried. Goldman Sachs held swaps from AIG that insured about $20 billion of securities. In August 2007, Goldman demanded $1.5 billion in collateral, arguing that the assets backing the securities were falling in value. AIG argued that the demand was excessive, and the two firms eventually agreed that AIG would post $450 million to Goldman, this person says. Late last October, Goldman asked for even more collateral, $3 billion. Again, AIG disagreed, and it ultimately posted $1.5 billion. Goldman hedged its exposure by making a bearish bet on AIG, buying credit-default swaps on AIG's own debt, according to one person knowledgeable about this move. Carrick Mollenkamp, Serena Ng, Liam Pleven and Randall Smith, *Behind AIG's Fall, Risk Models Failed to Pass Real-World Test*, WALL STREET JOURNAL, Oct. 31, 2008 at A1.
Nov. 9, 2008	Mr. Friedman, as Board Chairman, together with the Audit Committee Chairman, receives a courtesy telephonic briefing from NY Fed officers the evening of November 9, after the transaction has been structured, signed, and approved by the Board of Governors of the Federal Reserve System. The transaction is scheduled to be announced the following morning.
Nov. 10, 2008	FRB Press Release, *Federal Reserve Board and Treasury Department announce restructuring of financial support to AIG*, Nov. 10, 2008, *available at* http://www.federalreserve.gov/newsevents/press/other/20081110a.htm.
Nov. 10, 2008	AIG Press Release, U.S. Treasury, Federal Reserve And AIG Establish Comprehensive Solution For AIG, Nov. 10, 2008, *available at* http://media.corporate-ir.net/media_files/irol/76/76115/releases/111008.pdf.
Nov. 12, 2008	Wall Street Journal reports: "The banks that have sought and received collateral from AIG include Goldman Sachs Group Inc., Merrill Lynch & Co., UBS AG, Deutsche Bank AG and others." It also notes that these banks "will be compensated for the securities' full, or par, value in exchange for allowing AIG to unwind the credit-default swaps it wrote." Serena Ng and Liam Pleven, *New AIG Rescue Is Bank Blessing – Buyers of Insurer's Default Swaps Would Recover Most of Their Money*, WALL STREET JOURNAL, Nov. 12, 2008 at C1.
Nov. 14, 2008	ProPublica reports that "Under the government's latest deal, the Fed has helped AIG pay its obligations to those counterparties. The identity of those banks remains officially under wraps, but the Wall Street Journal has named a number of them: Goldman Sachs, Merrill Lynch, UBS, Deutsche Bank, Barclays, Credit Agricole, Royal Bank of Scotland, CIBC and Bank of Montreal." The article reports that billions of dollars in collateral payments were made by AIG to Goldman Sachs dating back to 2007. Paul Kiel, *AIG's Spiral Downward: A Timeline*, PROPUBLICA, Nov. 14, 2008.
Nov. 17, 2008	Reuters reports that of the 21 analysts covering Goldman Sachs, eight rated it a "buy" and only one analyst recommended selling the stock. Anurag Kotoky, *More analysts see bleak fourth quarter at Goldman, M. Stanley*, REUTERS, NOV. 17, 2008.
Nov. 20, 2008	Regularly Scheduled meeting of the Board of Directors of the NY Fed takes place. The Board minutes do not reflect any discussion of the AIG transaction.

As Revised

Chronology of Selected Events and Disclosures

Nov. 24, 2008	President-Elect Obama announces New York Fed President Timothy Geithner to be Treasury Secretary. Press Release, *Geithner, Summers among key economic team members announced today*, Nov. 24, 2008 *available at* http://change.gov/newsroom/entry/geithner_summers_among_ key_economic_team_members_announced_today/.
Nov. 25, 2008	Sterne Agee analyst Ada Lee gives Goldman Sachs a "buy" rating, saying the banks' shares were undervalued. Lee notes that Goldman's current stock price "reflects an unrealistically high probability of failure in light of the fresh capital raised from deep pockets and government funding programs." *Analyst rates Goldman, Morgan Stanley a 'buy,'* AP, Nov. 25, 2008.
Early Dec. 2008	Mr. Friedman asks about the status of the waiver and he is informed by New York Fed general counsel Tom Baxter that Fed rules as a matter of practice should be considered in abeyance while waiver decision is pending.
Dec. 10, 2008	Audit Committee of the NY Fed discusses the assets received from the bailout of AIG. Mr. Friedman did not attend the meeting.
Dec. 16, 2008	Goldman Sachs releases its 2008 Fourth Quarter Earnings Report, *available at* http://www2.goldmansachs.com/our-firm/press/press-releases/archived/2008/pdfs/2008-q4-earnings.pdf. The report includes detailed information about the Firm's revenue, expenses, and capital.
Dec. 16, 2008	During Goldman Sachs' Q4 2008 Earnings Call, Meredith Whitney of Oppenheimer & Co. notes that Goldman Sachs' "stated exposure to AIG has been immaterial," but asked whether the Federal Reserve's purchase of AIG securities had impacted Goldman Sachs' exposure. Goldman Sachs CFO David Viniar explained: "Our exposure has been immaterial. It is still immaterial. So there's been no change."
Dec. 16, 2008	Michael Wong, an equity analyst at Morningstar says: "We believe that Goldman Sachs is currently undervalued." *Goldman Sachs' Public Progress Report*, PBS, Dec. 16, 2008.
Dec. 17, 2008	Stephen Friedman purchases 37,300 shares of Goldman Sachs stock. Mr. Friedman also receives an award of 3,906 shares by virtue of his position as a Goldman Sachs director. The shares will convert to common stock following Mr. Friedman's retirement from the Goldman Sachs board. Stephen Friedman, Statement of Changes in Beneficial Ownership (Form 4) (Dec. 19, 2009).
Jan. 21, 2009	Federal Reserve Board Vice Chairman Donald Kohn grants Mr. Friedman a 1-year waiver allowing him to own stock in and be a Director of The Goldman Sachs Group.
Jan. 21, 2009	Mr. Friedman is reappointed Chairman and "Class C Director" of New York Fed by the Board of Governors of the Federal Reserve.
Jan. 22, 2009	Stephen Friedman purchases 15,300 shares of Goldman Sachs stock. Stephen Friedman, Statement of Changes in Beneficial Ownership (Form 4) (Jan. 26, 2009).
Jan. 27, 2009	Barron's reports Friedman's stock purchases. Teresa Rivas, *Goldman Director Makes $1 Million Buy*, BARRON'S, Jan. 27, 2009.
Jan. 27, 2009	Public announcement made that Mr. Friedman is reappointed Chairman and "Class C Director" of New York Fed by the Board of Governors of the Federal Reserve.
Jan. 29, 2009	Formal announcement made that William Dudley will replace Timothy Geithner as President of New York Fed.

Ms. NORTON. Thank you, Mr. Friedman.

Let's begin with Mr. Baxter.

Mr. Baxter, the committee notes that you have said publicly on a number of occasions that AIG, and not the Federal Reserve of New York, had the final say on disclosures. The committee has, however, in its possession an email, I believe it is up there on the display, that was obtained by subpoena. It involves a senior person in your office, and the words said are, "any public disclosure by AIG was still subject to FRS approval," Federal Reserve Service approval. That sounds pretty much like the Federal Reserve has the final approval with that kind of statement.

If what you say about AIG having the final decision is true, why did a top New York Fed employee say that the final approval, in effect, rests with the Federal Reserve?

Mr. BAXTER. Madam Chairman, as I look at that email, I don't see it being addressed to me. So I will have to speculate as to why the author of that email——

Ms. NORTON. Who do you think it was addressed to, Mr. Baxter? You know, you don't just send emails in the air.

Mr. BAXTER. I can't read it well enough, Madam Chair, to tell you, but it doesn't look like it is addressed to me. Madam Chair, I am willing to speculate, though.

Ms. NORTON. Well, since you raised the issue of who it is from, Steven Massari to Sarah Dahlgren. It is your top people. Your proxies speak for you, do they not?

Mr. BAXTER. They are not only very, very senior people. They are also very diligent people. And with respect to the email, Madam Chair, it doesn't refer to securities disclosure. It refers to a public disclosure by AIG, so I would point that out as one item.

With respect to AIG's securities disclosures, those are AIG's legal obligations under our securities laws, given that AIG was then and is now a publicly traded company. So in the first instance, AIG has a responsibility to comply with our securities laws. And that is the starting point.

Now, it is true that AIG shared its securities law disclosures with the Fed. And it is true that the Fed commented on those draft securities law disclosures of AIG. Our purpose in making those comments was twofold: first, to assure accuracy; and second, to protect the taxpayer interest. But at no point, Madam Chair, did we ever interfere with a mandatory obligation of AIG to report to the SEC in a securities filing. It was always for the two interests that I mentioned, the interest of accuracy and the interest of protecting the taxpayer interest that we commented on AIG's public disclosures.

Now, it could not——

Ms. NORTON. Board approval is a very troubling word here. It implies what it says.

Mr. BAXTER. It is, Madam Chair, and it could not be for an AIG public filing and approval because that legal obligation with respect to AIG's securities filings as a public company is AIG's. It cannot be delegated to someone else.

Ms. NORTON. Agreed.

Mr. BAXTER. Not even someone at the——

Ms. NORTON. Agreed, but it looks, though, it looks as though a very powerful agency was saying otherwise. I agree with what you say, but that is not what the email said. Perhaps you can see why it makes it look as though the Federal Reserve of New York is not being up front with the American people here behind the scenes where these emails that put the Federal Reserve in a position that you yourself indicated is not a position it can have under law.

Mr. BAXTER. Correct.

Ms. NORTON. Mr. Barofsky, perhaps you can help me. I am sitting here listening to this testimony and I still cannot understand. I need to understand, for a moment put yourself in the position of the parties, why you think AIG's counterparties were paid 100 cents on the dollar?

Mr. BAROFSKY. Well, I think that, you know, it is hard to put myself into the shoes of either the counterparties or the Federal Reserve, but my understanding of the discussions, I certainly understand why the counterparties wanted to be paid 100 cents on the dollar.

Ms. NORTON. Of course, but why would the government want to do that? I mean, you cannot assume in a situation like this that somebody wants to do evil or to cheat the taxpayers. We are trying to find, get beneath the appearance, trying to place ourselves at the table with the parties, including the government, including the Federal Reserve, including AIG.

So you yourself in your testimony lay out what had just occurred. Why would that procedure not be used?

Mr. BAROFSKY. I cannot give you an answer to that question. I think that if that effort and that tone were there, Mr. Baxter could answer that question. Probably Secretary Geithner could best answer that question.

Ms. NORTON. Well, I mean, again, if you have to assume the best and not the worst, then what would be the best reason for not using the Government's bargaining power?

Mr. BAROFSKY. I really cannot imagine. I think that, again, accepting the policy limitations that they imposed upon themselves—and we don't accept them necessarily in the audit—but even accepting them, it seems to me that taking the effort—apparently, Secretary Geithner at the time was frequently speaking to the CEOs of many of these counterparties. It seems that just putting a little extra effort in trying to communicate the importance of this. I mean, negotiations were ongoing. It is not as if, as somebody may think, that they made no effort in negotiations. There was some effort negotiating.

Ms. NORTON. So there was effort, so, you know, when you say that they said, "would you accept 100 cents on the dollar, less than 100 cents on the dollar," why, anybody would answer "no" to that question.

Mr. BAROFSKY. The surprising thing is that one of them did answer "yes," and that wasn't——

Ms. NORTON. And why do you think he answered "yes" and the others answered "no?"

Mr. BAROFSKY. I think they were willing to negotiate because I think that, you know, if you look at it from——

Ms. NORTON. Did he know the others had answered "no?"

Mr. BAROFSKY. Well, he said "yes" only as long as all the others would say yes. So his idea was that we would do——

Ms. NORTON. Well, why didn't he stick with the others? I mean, there must have been some—Mr. Baxter?—why would—you know, if you see that there is solidarity here and maybe you can get the government where you want it, why would one person say yes? He must have known something. He must have felt something for the country? Did he feel something for the economy that made him do it? Is he a patriot and the others not?

Mr. BAROFSKY. I think that there was, you know, this was UBS, and I think there probably was a recognition that the Federal Reserve had done so much for the global economy, and the American taxpayer—putting the American taxpayer who had literally taken the entire global economy on its back and was supporting not just the U.S. institutions, but the global systemic risk that the sacrifices the taxpayer had made.

And that, I think, is a powerful argument in the context of negotiations if it is made clear how important it was to the American decisionmakers, to the principals. And I think that perhaps, I don't want to crawl into the mind of the UBS, but there was a willingness to engage in these discussions, but as long as all the others. And because seven of the eight had said no, the Federal Reserve essentially shut down those negotiations.

But I think it is a very fair question to say why not do something similar to what was done just a couple weeks before in Washington with respect to the Capital Purchase Program, which is, again, those were not compelled transactions, it was ultimately a voluntary transaction, but the negotiations, if you will, were conducted in a very, very forceful manner that made it very clear that this was an issue of national importance.

Ms. NORTON. So I would ask you the same question, Mr. Baxter. One of the reasons I feel so angry at the banks and at the government is that this is a commonsense question that anybody would ask without being very learned or very practiced in negotiations. So could you give us your answer?

Mr. BAXTER. And I think, Madam Chair, this is a key question. The key question is, why didn't the Federal Reserve act successfully to get a concession of perhaps——

Ms. NORTON. Is your mic on, sir?

Mr. BAXTER. I think it is.

Why weren't we successful in getting a concession from the counterparties? Why wasn't AIG successful in getting a concession from the counterparties, because that was the situation? And it is related to bargaining power.

Now, typically when a debtor is trying to restructure a debt with a creditor, the bargaining power that the debtor gets, Madam Chair, is from the threat of bankruptcy. This negotiation with the counterparties was taking place in the fourth week of November 2008. So how would the threat of bankruptcy have played during that particular period of time? And of course, Madam Chair, you know that the Federal Reserve had already interceded to save AIG from bankruptcy on September 16, 2008, only 6 weeks before.

So what about the bankruptcy threat? And I have three responses. First, that threat was not credible, given the actions of

September 2008. Second, that threat of bankruptcy was not true. We were not prepared to put AIG into bankruptcy in November 2008, and we don't misrepresent situations in negotiations at the Federal Reserve.

Ms. NORTON. But the threat was there. Excuse me. The difficulty and the bargaining positions were there. So I still don't understand why ask a simple question didn't proceed, with business as usual, as if you weren't holding that threat card.

Mr. BAXTER. And I am trying to explain exactly why we had no bargaining power with respect to the bankruptcy risk. The first is it wasn't credible. The second is it wasn't true and it would have been unethical for us to suggest otherwise. And the third is it would have been counterproductive because the biggest threat we were facing at that point was the threat of the credit rating agencies downgrading.

Ms. NORTON. Mr. Baxter, I understand that nuclear bomb threats are not credible. And I can understand your argument as to the insolvency.

Mr. Barofsky, now, it is true that when you comment and you tell somebody, you know, you are going to kill them, and you know for sure that you are not, and they know for sure you are not. Then the question becomes, what is the next step after the nuclear bomb threat?

Mr. BAROFSKY. I think there are two things. First of all, what I was suggesting, that the principals got involved in negotiation. I wasn't suggesting that they threaten bankruptcy. My comparison to what happened a couple of weeks earlier was, again, presuming all the restrictions that Mr. Baxter and Secretary Geithner had put on themselves, including not wanting to threaten bankruptcy. So first of all, I think that what I was, when drawing this comparison, I wasn't suggesting that they do.

As to the complete absence of leverage, again, I think you have to look at this in the context of what the situation was, what the position of U.S. Government officials explaining how important this was, much like they had 2 weeks earlier. And I don't think that they needed to threaten bankruptcy.

However, as Secretary Geithner noted this morning, there was a very serious concern at the Federal Reserve and in the markets that there was going to be a downgrade of AIG, a downgrade that Secretary Geithner and the Federal Reserve have indicated to us, would have resulted in AIG going into bankruptcy despite the best efforts of the Federal Reserve. There is a limit on how much money, perhaps, the Federal Reserve was willing to print at some point if bankruptcy was triggered.

And I think that, again, without threatening bankruptcy, I think that if there was a negotiation, if everyone was in the room, the Federal Reserve could point to the fact that there is a possibility of a downgrade. They could point to what the market was treating AIG's debt at the time. The credit default swaps were through the roof. There was fear in the market that AIG would default. And again, without threatening the bankruptcy, could point out the fact that if there was not a resolution, if they didn't agree to a haircut, it may be difficult for the Federal Reserve to get Board approval, for example, to pay 100 cents on the dollar. They had not yet received that approval.

What I am saying is that there is a whole different range of options in that negotiation that could have occurred had they simply brought everyone in the same room and if it was made a priority, if there was a level of effort across the board.

I can't tell you if it would have worked. I have no idea if it would have worked.

Ms. NORTON. Well, have you ever heard 100 cents on the dollar being given in the kind of situation like this? Isn't that rare as a way to come forward when you see a desperate situation on the other side? Surely, some gradations down from that were in order.

And I guess I should ask Mr. Baxter. The puzzling thing is to come up with 100 cents on the dollar without proceeding through some other process until you maybe had to get there. We don't see, the committee does not see how you—and is bothered by the spontaneous nature of the acceptance of the notion that the government had to pay 100 cents on the dollar. We have hardly heard of a negotiation in our lifetime when that is what two unequal parties at the table end up doing, no concession, 100 cents on the dollar.

So perhaps you can tell us why what Mr. Barofsky says at least some sense, yes, of course, you are not going to put them into bankruptcy. We do not question nearly as much the bottom line here as we question how you got to that bottom line.

Mr. BAXTER. Well, because we couldn't use the threat of bankruptcy, Madam Chair, one question was could we use our regulatory or supervisory power? And we considered the answer to that question "no," because that would have been an abuse of our power. And the reason we felt that is it wasn't using the supervisory power with respect to an institution to get it to do something to enhance its safety and soundness, for example, like raise more capital.

If an institution doesn't do that, and it is appropriate if the Fed believes there is insufficient capital to use a promise or a threat perhaps of enforcement action to induce the institution to take that action, that was not the case here. Here, the suggestion is we use our regulatory power to cause a counterparty to give up property in the form of a concession.

So it is not using the regulatory power for the purpose intended by law. It is using the regulatory power as a promise or a threat to extract money from someone. And that raises all kinds of considerations that are not consistent with the rule of law.

And just another point, Madam Chair.

Ms. NORTON. You apparently didn't think you had to change the regulatory power in order to deal with Bank of America. Somehow you would have to go back, change the law in order to deal with AIG.

Mr. BAXTER. Well, Madam Chair, remember what happened when we asked the two French banks, SocGen and Calyon, if they would give a concession. Their first answer was no, and then they were supported in that negative answer by the French Banking Commission. So that happened with the two French banks.

You also asked earlier about UBS. Now, UBS said, "we might consider as much as a 2 percent concession, but only if everyone does it, everyone else does that as well.” And so there was a fairly effective blocking action there by UBS.

Now, on the point that participating in the benefits of all of the Federal Reserve’s and the Treasury’s action in combating the financial crisis, with respect to UBS, Madam Chair, remember UBS had already been rescued by Switzerland in the financial crisis.

So again, in UBS, we are dealing with UBS. We asked them if they would consider a concession. You know what their answer is, but it is a hard case to make that they owed the United States a favor when Switzerland had already come to their rescue.

Ms. NORTON. Thank you, Mr. Baxter.

I am going to move now, since I have had more than the allotted time because it took you all so long to get back, I am going to move to the ranking member.

Mr. ISSA. I thank the chairwoman, and I certainly think that this was a good case for your not necessarily wanting a floor vote today.

Ms. NORTON. But not tomorrow.

Mr. ISSA. But not tomorrow.

Thank you, Madam Chair.

Mr. Baxter, I didn’t know who you were after 30 years of loyal service until a few days ago, so forgive me for maybe now playing total catch-up. Your old boss, now-Secretary Geithner, spoke glowingly about the staff and the hard work and the people involved. But we now believe and understand that a staff report was done within the Fed that said “let AIG go bankrupt,” and that was never, ever brought before the Board. In fact, Chairman Bernanke pulled it so it would not be considered by the broader Board of Governors.

Are you familiar with that study or report?

Mr. BAXTER. I am not.

Mr. ISSA. You are not. So he kept it from a person who was—these emails show you were at the center of all of this. He kept from you his own staff’s decision. Chairman Bernanke did not trust his own Governors or even the New York Fed’s inner circle with a recommendation that said let them go bankrupt.

Does that surprise you?

Mr. BAXTER. First, ranking member, I am the general counsel of the New York Fed. The chairman——

Mr. ISSA. But all that question was in the New York Fed. It was a study on behalf of the New York Fed.

Mr. BAXTER. I don’t know the study, and I am sorry I don’t.

Mr. ISSA. OK. Well, with any luck and with the indulgence of the Chair, we will get discovery on that. As of right now, all I have is a whistleblower and one Senator who confirmed that it exists, but has said on CNBC that he can’t release it, even though he thinks it is damning.

Additionally, you are familiar with Schedule A of the documents. OK. So this unredacted form shows 57773 and some alpha numeric after that. It then shows that Deutsche Bank would be the counterparty recipient, the breakdown. Basically, these are sort of who owns the bonds, to put it in terms the American people would understand.

Are you familiar with this document called Schedule A? It was delivered from the Fed.

Mr. BAXTER. This was Schedule A, the shortfall agreement?

Mr. ISSA. Yes.

Mr. BAXTER. Yes, I am familiar with that.

Mr. ISSA. Are you familiar with the cover-up that AIG, with the insistence of the Fed, clearly perpetrated by getting this made confidential and not disclosed to the public until 2018, that work continuing until may of this year, or last year?

Mr. BAXTER. Congressman, there was no cover-up. I can explain the processing of the Schedule A.

Mr. ISSA. Well, if you can just briefly tell me the first part, which is are you familiar with the work that went on to seal this from being disclosed in public SEC filings at least until 2018.

Mr. BAXTER. I am familiar.

Mr. ISSA. OK. And in a short way, do you think that is right or wrong?

Mr. BAXTER. I think all of the conduct was perfectly appropriate.

Mr. ISSA. OK. Well, I am going to leave that because although I don't agree, ultimately I just wanted that answer and we will see in time on other people.

Can you put up slide 23 please?

Can you please explain what happened following your receipt of an email from Marshall Huebner? And did AIG ever make this filing with the SEC?

Mr. BAXTER. Would you like me to explain?

Mr. ISSA. Please, as briefly as possible.

Mr. BAXTER. This concerned a salary increase for the chief financial officer of AIG, and Mr. Huebner was concerned about that salary increase. I was also concerned about that salary increase. And as a result of our collective concern, I had conversations with AIG, and the chief financial officer in question decided that he really did not want the salary increase at this time. The salary increase was withdrawn.

Mr. ISSA. OK. So by talking him out of it, it didn't have to show up in public filings, so it was no harm, no foul in this case?

Mr. BAXTER. It had nothing to do with the public filing. It had everything to do with we didn't think this was appropriate.

Mr. ISSA. OK.

Mr. BAXTER. The salary increase.

Mr. ISSA. A last question for you, and then I want to quickly go to the SIGTARP. Do you know of a compelling legal authority that would have prevented AIG from going bankrupt? In other words, did the Fed have the authority to let them go bankrupt? Because Secretary Geithner has implied that he didn't have any options and he didn't have the authority to do anything but what he did.

That is pretty much ayes or no. Did you or anyone at the New York Fed, to your knowledge, in fact do a study or come up with a legal opinion that said you can't do anything else except let them go bankrupt or do this, and you can't let them go bankrupt?

Mr. BAXTER. First, we were not the supervisor of AIG on September 16, 2008, so we had no supervisory responsibility.

Mr. ISSA. No, no, but my question is since Secretary Geithner was there and said there was no other choice, your boss made the call. Do you know of a legal opinion that he was given or that exists today as to that?

Mr. BAXTER. Well, I was his chief legal officer, and I would say then what I say now, and that is we need a resolution statute in this country to deal with institutions as systemically significant as AIG. We didn't have that tool in September 2008 and we still don't have that tool, Congressman.

Mr. ISSA. OK.

Mr. BAXTER. And we really need it.

Mr. ISSA. But, you know, I am going to ask this for 2 minutes, quickly, to sort of counter the very long time, but I will be very brief.

Mr. ISSA. I thank the chairman.

Chairman TOWNS. [presiding]. I yield the gentleman 2 minutes.

Mr. ISSA. Mr. Barofsky, your report directly contradicts so much of what we are hearing from people that were there or are there as to whether we will get paid back. Let me break it down to just two questions, and then take the rest of the 2-minutes for your answer.

One, is it true that we are just not going to get paid back by anyone's reasonable estimation certain funds? And two, had we used other means to underwrite AIG such as we will buy out that at a discount or we don't buy them? We will guarantee or give, or buy at discount, you decide whether you want our AAA rating versus actually getting the transfer at a time when these banks wanted a transfer?

If any of these other techniques that you are now aware of that logically could have been used, would we be in as bad a situation of not getting paid back as we are?

And then, please elaborate on what we are seeing of what we are not going to get paid back that flies, and that doesn't even include, by the way, the idea that the moneys come back and it is being respent in other ways. But just as to your knowledge, can you give us as much knowledge, as much time as we do have to answer that?

Mr. BAROFSKY. Sure. Ranking Member, I just want to take the chance that is in my initial testimony to thank you and the chairman for your support of our organization and for the leadership and the tenacity that the two of you and this committee has shown in bringing transparency to the AIG bailout. The Treasury's own calculation is when they did their financial statement at the year-end, September 30, 2009, projected a more than $30 billion loss on its AIG investment.

When you are looking at these counterparty payments, you can't look at just one part of them. They were basically in two chunks, if you will. There is the Federal Reserve loan to Maiden Lane III, which purchases securities. This is about $29 billion. And the rest were counterparty payments, the balance of about $33 billion that AIG had previously made. So there is a total of about $62 billion.

Now, with the chunks that the Federal Reserve lent to Maiden Lane III, that portion, which we have been hearing about, how that is on track to be paid back and the taxpayer may actually, and the Federal Reserve Bank of New York may actually make a profit on that. I see no reason to think that is not true. That may very well be accurate, that one piece of it.

However, the other piece, and these really are two sides of the same coin, and we have been critical of trying to separate that out and only looking at the Federal Reserve piece and saying, "oh, because that is going to get paid back, it is a profit," that other part is part of the projected $30 billion loss.

So one of the reasons why we are so critical is that if you just say, "oh, on these transactions, where the Federal Government, the taxpayer, is on track to be made whole," for someone who is not as familiar with the intricacies of these transactions as we all are, you would get the mis-impression that the counterparty payments, the decision to pay 100 cents on the dollar, is going to leave the taxpayer whole.

And by Treasury's own calculation, you can't separate that $30 billion of anticipated loss from these transactions because the money that AIG paid came from a loan from the Federal Reserve, a separate loan that was then paid down with taxpayer money through the TARP. So I think it is——

Mr. ISSA. I am sorry, so I think it is very difficult and I think it is inappropriate to separate those two out.

Thank you, Mr. Chairman.

Chairman TOWNS. I now yield 5 minutes to the gentleman from Massachusetts.

Mr. LYNCH. Thank you, Mr. Chairman.

I want to thank the witnesses for your willingness to help the committee with its work.

Mr. Barofsky, we have been going back and forth with Secretary Geithner and Secretary Paulson earlier today about the decision to pay the derivatives, well, credit default swaps that were entered into between AIG and Goldman Sachs and a handful of other companies. The position of Secretary Geithner is that he didn't have any other tools other than paying 100 percent of the value, 100 cents on the dollar, or allowing AIG to go into default and bankruptcy. And at least the testimony of Mr. Paulson is that he was not there, and I find that mystifying.

But in your own impression and reviewing the record here, was there any opportunity for Secretary Geithner, the Treasury, the Fed, to negotiate a haircut with Goldman Sachs instead of paying them at par value, and thereby saving the American taxpayer possibly billions of dollars?

Mr. BAROFSKY. Yes, and I think that as the Federal Reserve and the Secretary acknowledge, the whole plan that the hope from the Federal Reserve was to attempt to negotiate a haircut. So if there was an agreement among the parties to pay, to accept less than par, that obviously wouldn't have violated any of the policy concerns that have been described. And I think very much these negotiations could have been conducted in a different way, a more forceful way.

The comparison that you cited to Secretary Geithner earlier and which is discussed in our testimony is looking back to the Capital Purchase Program when the nine banks were summoned to Washington, DC, and, as mentioned in my testimony, that is a pretty good example of what could have been done.

There, of course, it was the principals that were involved in the negotiation for both sides, whether it was Secretary, then-President

Geithner, Secretary Paulson, Chairman Bernanke on behalf of the government, and the chief executive officers of the nine banks on the other side. That didn't happen with AIG. The forcefulness of those negotiations, being told that this was important to the American people.

Now, I am not suggesting that threatening to pull their license or using regulatory authority to punish those that didn't participate, but emphasizing how important it was to policymakers of the U.S. Government. That didn't happen with respect to AIG. And indeed, again, these were conversations that were done largely over the telephone with mid-level executives.

Those nine executives were summoned to D.C. for the TARP, and they were put around the table. And that communication, that this is really important and we could, you know, I can continue to speculate and give about 9 or 10 other things that could be said, all I think within the confines of the Fed's policy considerations.

Now, we have been somewhat critical of some of those policy considerations, and you know, we disagree with some of them, as reflected in the audit. But I think that what is bothersome is that even if you accept all of those concerns, they could have just tried a little harder, and maybe it would have been unsuccessful. We don't know. But as I noted in my testimony, we recently spoke to the French regulator, and they said if the negotiations went something like that, they would at least be willing to engage. And we know that UBS would have been willing to engage.

And we don't know what the reaction is of the other potential counterparties because that telephone conversation from then-President Geithner or then-Secretary Paulson or Chairman Bernanke saying, "hey, this is important; we want to you to be involved," we know they were talking to these CEOs on a regular basis, but this wasn't elevated to that level, and we will never know what the result might have been. But it may have resulted in saving the taxpayers billions, if not tens of billions of dollars, but we just don't know the answer.

Mr. LYNCH. OK, thank you.

Mr. Baxter, maybe you have been asked this question before, but in terms of the decision to make the payment at 100 cents on the dollar, were you part of that discussion?

Mr. BAXTER. I wasn't in the discussions with the counterparties, Congressman, but I was part of the supervisory team.

Mr. LYNCH. How did you arrive at that? Could you tell me?

Mr. BAXTER. I can try. First of all, there was a critical deadline, Congressman, of November 10th, and that was the day that AIG was going to announce a $25 billion loss in its 10-Q for the third quarter, so we were looking at that. And we were being told by the credit rating agencies that unless something happened with respect to the credit default swaps on or before November 10th that there was a strong probability of a downgrade.

Now, a downgrade would have been catastrophic. It would have brought us back to where we were in September, on the brink of an AIG bankruptcy. So from those of us who were working at the New York Fed, we looked at that as a hard deadline. And the execution risk of failing to get the credit default swaps torn up by that date was it would have put us back on the brink of bankruptcy.

So that was the risk of deal failure. That was the execution risk, so we had to get the deal done.

AIG had been unable, as Mr. Habayeb has testified, to get those credit default swaps torn up. On November 6th, Congressman, we got formal authorization from Stasia Kelly, who was then AIG's General Counsel, to take over and see whether we could get those credit default swaps terminated by deadline. So we were operating against the clock to do that.

Our choices were should we push for concessions and try to use whatever leverage we had to get those concessions? Or should we simply go to par which would apply to every counterparty, and the way par works is you offset the collateral that these counterparties had been pulling out of AIG against—you offset that collateral against the par price of the bonds.

So those were the weighing of the risks as we faced them. And on the one hand, failure to get a deal on or before the 10th would have brought us back to the brink of an AIG bankruptcy. So the risk was in pushing for concessions of perhaps 2 percent. We risked billions of further Federal Government assistance.

Now, what happened? We asked eight counterparties about concessions. Seven said "no." Two of those seven were French, and they were supported by the French Government in their refusal. The one that said "perhaps" was UBS. It said perhaps up to 2 percent, but we need to be treated just like everybody else.

So had we continued to use whatever leverage we had, and as I said earlier, we didn't have much, we risked losing the deal by November 10th, and that would have brought us right back to September, to the brink of an AIG bankruptcy and to catastrophic systemic consequences that would have resulted.

That balancing led us to see that the solution would be to go with no concessions. We brought that to President Geithner. He agreed, and that is what we did, but we brought it home by deadline. We got it done by the 10th.

Chairman TOWNS. The gentleman's time has expired.

I now yield 5 minutes to the gentleman from Indiana, Mr. Souder.

Mr. SOUDER. Did I hear, Mr. Baxter, did you say that Mr. Geithner signed off on paying at par as part of that decision?

Mr. BAXTER. He did.

Mr. SOUDER. I didn't have that impression earlier, but maybe I misunderstood something.

I am not sure who to ask this particular question to first, but let me ask Mr. Barofsky. One of the questions here is, my understanding was, to avoid the—and part of the question for the secrecy, was to avoid the risk of the rating agencies downgrading the securities and bonds. Is that true? Is that your impression?

Mr. BAROFSKY. The Federal Reserve has cited as one of the justifications for paying the counterparties at par was one of the concerns about the effect on ratings agencies and the impact.

Mr. SOUDER. And why hadn't they already been downgraded?

Mr. BAROFSKY. Well, they actually had been downgraded up until that point, but——

Mr. SOUDER. Do you believe they were keeping up? In other words, in the many hearings that you have been here and so on, it seems to me that to have a private economy work, one thing has to happen because, you know, CalFed, or whatever the big insurance for State employees there, is the biggest, I guess, investor, and he said he has only got a couple of people to track. If those rating agencies aren't accurate, the whole system collapses. And it seemed to be questionable whether they were moving fast enough in the economy to downgrade it. And in effect here, a partner in the Fed was trying to help disguise it.

Mr. BAROFSKY. I mean, ultimately, one of the observations in our audit is the outsize influence the credit rating agency had throughout this process. As Mr. Baxter just stated, it was basically the rating agencies that were holding the gun to the head of the Federal Reserve, giving them the perception they had to move so quickly. It was the rating agencies that gave the fear to the Federal Reserve, and I am sorry, I don't mean to, I am paraphrasing Mr. Baxter, but that fear that AIG would be put into bankruptcy, that was a legitimate fear that the Federal Reserve had because of the results of the rating agencies.

And of course, so much of the lead-up to AIG's problems were the result of the rating agencies. First, over-valuing the CDOs and the bonds that underlie the credit default swaps, and then throughout the process. Indeed, it was the rating agencies who were ultimately looked at the original deal that the Fed brokered with AIG and the high interest rate, and determined that, too, would lead to an eventual downgrade. So, yes, they had an outsize role in this for certain.

Mr. SOUDER. Mr. Baxter, my question to you would be how can a free market economy work if the Fed tries to manipulate the rating agencies by pumping money in and trying to conceal that?

Mr. BAXTER. We never tried to manipulate the rating agencies, Congressman. We took their observations as they gave them to us, never tried to lever them in terms of what they were going to do with respect to AIG. Instead, what we tried to do was to restructure AIG to avoid a downgrade.

Now, in the context of November 10th, and this is an important point with respect to the credit default swaps, had that downgrade occurred, many of the counterparties would have had a right to terminate their credit default swaps, which would have enabled them to keep the cash collateral posted and the bonds. And that is a critical piece here because the way we restructured these credit default swaps, the Fed took the bonds into our vehicle, Maiden Lane III. And remember, the bonds had diminished in value from par to approximately half, and the counterparties had gotten collateral for that diminution in value.

As those bonds, which we now have in our vehicle, as those bonds come back in value as our Nation emerges from the worst financial crisis in 70 years, we capture that value in a Federal Reserve vehicle. And so it is the offset, if you will, in broad terms, conceptual terms, to the collateral that was posted.

And so this is another important feature of the restructuring that the Fed did which was far, far better than the alternative of allowing there to be a rating agency downgrade and those catastrophic consequences.

Mr. SOUDER. And why did you want to conceal that?

Mr. BAXTER. Never wanted to conceal that, Congressman. It is, and we tried——

Mr. SOUDER. Is it inaccurate to say that you asked for special conditions where markets wouldn't be able to see, for fear they might speculate if they saw that you were taking this position?

Mr. BAXTER. Well, first with respect to the schedule A, to the shortfall agreement which had the counterparty names, the CUSIPs, the tranches. It was never the intention of AIG or the Fed for that schedule to be filed with a shortfall agreement. So there was a misunderstanding in the beginning, I think, as to why that wasn't attached.

Now, the Commission came back and said, we need that exhibit attached, and then we made an application for confidential treatment because we thought that information would hurt the taxpayer interest in our vehicle. Now, the information I am talking about are the counterparty names, the CUSIP numbers identifying the bonds we hold, and the tranches. After the hearing that occurred before this committee in March, we and AIG changed our view on the counterparty names.

So the only information today that is confidential with respect to the schedule A is the CUSIP numbers and the tranches, the identifying information for the cards, if you will, that the Fed holds in its hand in this vehicle. That is what we are keeping confidential now, and for the right reasons because we are worried when we sell out that portfolio that if the street knows what we are holding, it will hurt the taxpayer interest. That is the only reason. It is not a cover-up.

Chairman TOWNS. The gentleman's time is expired.

I now yield 5 minutes to the gentleman from Maryland, Mr. Cummings.

Mr. CUMMINGS. Thank you very much, Mr. Chairman.

Inspector General Barofsky, thank you again for all the work you and your team have done over the last year. It has been simply invaluable.

When I and 26 of my colleagues wrote to request that you conduct an audit of the issues before us today, our main concern was the decisionmaking process leading to paying AIG's counterparties at 100 percent par value. However, after Bloomberg and the New York Times published emails surrounding the disclosure, questions began to emerge about how the events surrounding the Maiden Lane III transactions were disclosed to the SEC.

One of the first things I did was send you a letter asking whether your staff already knew about the emails that were released to the press and did these emails affect the conclusions that you reached in your audit. I was also interested in whether you planned to open the audit.

You responded quickly, as you recall, saying that it was not your policy to comment on open investigations. Is that correct?

Mr. BAROFSKY. Yes.

Mr. CUMMINGS. All right. And I want to clarify, in your office "audit" and "investigations" are different tasks conducted by different personnel in different divisions. Is that right?

Mr. BAROFSKY. That is correct, generally speaking.

Mr. CUMMINGS. OK. And what are the missions of those divisions?

Mr. BAROFSKY. Sure. Audit, as you know, under EESA, we have the responsibility to both audit and investigate all actions taken under the TARP. The best way I think to think of audit, it is almost investigation without the presumption that there was a crime or a violation. It is a review, a historical review of what occurred, and in looking to see what went wrong, what went right, and explaining, bringing basic transparency and making recommendations.

Our Investigations Division is a law enforcement agency. We are like the FBI for the TARP. It is populated generally by special agents who have full law enforcement authority, guns, badges, and the authority to make arrests. We also have attorney advisers and support personnel. And when we move something into the Investigations Division, it is because we are taking a look to see if there was misconduct. If there is some reason or there is an allegation or we suspect in certain cases where there is a crime or even a civil violation, we do support civil investigations as well, we move it over into that section.

So with respect to your letter and the request, we didn't receive many of the documents that this committee received, including those documents, as well as some other documents that pertain very directly to some of the issues directly addressed in the audit.

Mr. CUMMINGS. Does it surprise you that you didn't receive them when you would, I mean, now looking back?

Mr. BAROFSKY. Some of the documents I am extremely surprised that we didn't receive. And that is why we are conducting a new investigation to determine what the circumstances were of why specific documents that we requested were not provided to us.

Mr. CUMMINGS. So an open investigation is not the same as an open audit. Is that right?

Mr. BAROFSKY. That is correct, sir.

Mr. CUMMINGS. And I assume you cannot say whether the open investigation is civil or criminal. Is that correct?

Mr. BAROFSKY. Well, an investigation at this stage in particular, we are just starting out. We are just taking a look and see where it goes. If it does result in our belief for a referral for civil or criminal prosecution, we would do that. We would then interact with the Department of Justice. We don't have prosecutorial authority.

If we determine otherwise, especially with respect to these investigations, we have the option of preparing an investigative report which we will provide to you and this committee reporting on our findings.

Mr. CUMMINGS. Can you tell us what the timeframe is for this? Do you just have to take your time and figure that one out?

Mr. BAROFSKY. I mean, for us to do this right, 250,000 pages of documents that this committee received, we also received. That is going to take us some time because we really can't determine what we didn't receive until we go through literally every page of those documents.

And given the significance and importance of this matter, I usually drive my agents pretty hard and ask them to move very, very quickly. In this instance, I told them above all to move quickly, but we need to be very thorough and very accurate. And that will be followed, as all investigations, by a series of interviews once we get our hands around the documents.

So I hesitate to put a time.

Mr. CUMMINGS. I understand. Bloomberg reported this morning that you are, "probing whether the New York Fed improperly limited the release of information about payments to AIG's bank counterparties." Is this correct or can you comment on that?

Mr. BAROFSKY. Yes. We also have opened a probe into some of the allegations that came here. And again, I really want to stress that when we open an investigation, we are not presuming misconduct or anything like that. It has been suggested that there was misconduct. Again, so what we are doing, it is our job, our responsibility, our statutory responsibility when such issues are raised, we have to go look at it.

And as I said, if everything was done in a legally correct manner, we will report that.

Mr. CUMMINGS. I see my time is up.

Thank you, Mr. Chairman.

Chairman TOWNS. Thank you very much.

I now yield 5 minutes to Congressman Bachus.

Mr. BACHUS. Thank you.

Mr. Barofsky, I am going to ask you this question. You know, Secretary Geithner says that they didn't disclose some things, but now they have come, they have fully disclosed everything and they are trying to inform the American people.

However, I think his testimony today appears to mislead the American people, and let me ask you about that.

On page 10 of his testimony, he is talking about the AIG bailout. We paid the fair market value at the time for the assets. Essentially, what the Federal Reserve did was to purchase these securities from the counterparties with a par value of $62 billion for a purchase price of $27 billion. That is not true, is it?

Mr. BAROFSKY. It is partially true.

Mr. BACHUS. Partially true. What they don't say is they got $27 billion of taxpayer funding and they got to keep $35 billion worth of collateral.

Mr. BAROFSKY. I mean, it is true in addition to the $27 billion that came from Maiden Lane III, all that other AIG collateral that they previously had been paid, which was made possible largely by the other loan from the Federal Reserve, which was back-filled $40 billion by taxpayer money. And I think in the Secretary's full testimony, he does acknowledge that there is an AIG loss. What we cite in our testimony was a statement that was put out by Treasury which was completely unbalanced and gave the impression that the taxpayers would be made whole because of that narrow issue of Maiden Lane.

Mr. BACHUS. Well, that is actually what this statement this morning to me says that they purchased securities with a par value of $62 billion for a purchase price of $27 billion.

Mr. BAROFSKY. It is literally true in the Maiden Lane III facility. That is what occurred. It is literally true.

Mr. BACHUS. Yes. He said in the end, the prices paid for the securities were their fair market value. That is not true either, is it?

Mr. BAROFSKY. Well, again, with respect to the Maiden Lane III part of it, it is literally true, but to look at these transactions as a whole, the counterparties did receive 100 cents on the dollar for those securities and for tearing up the credit default swap contracts. So the total compensation when you include the collateral they were able to keep was effectively par value.

Mr. BACHUS. Because the counterparties, they received $62 billion in all, $27 billion of it paid directly from the special purpose vehicle.

Mr. Baxter, Mr. Friedman, you would agree with that? They received $27 billion from the special purpose vehicle, is that correct?

Mr. BAXTER. I think it is very important, Congressman Bachus, to understand that we paid for multi-sector CDOs with a par value of $62 billion.

Mr. BACHUS. Right.

Mr. BAXTER. Our vehicle paid $29 billion.

Mr. BACHUS. $29 billion, all right.

Mr. BAXTER. Now, $27 billion went to the counterparties; $2 billion went to AIG. Another important aspect of this is then we received those multi-sector CDOs into our vehicle.

With respect to the cash collateral that AIG posted, this is important. This is important.

Mr. BACHUS. But what I am saying, to say that——

Mr. BAXTER. We now can recapture that because as those multi-sector CDOs come back in value as our Nation emerges from the worst financial crisis in 70 years——

Mr. BACHUS. I understand about the worth, but what I am saying——

Mr. BAXTER. Then the value comes back.

Mr. BACHUS. But what I am saying, it was $27 billion and then it was $35 billion worth of collateral that the counterparties were allowed to keep.

Mr. BAXTER. Which they were legally entitled to.

Mr. BACHUS. Oh, I understand that, but what I am saying to say that this, you know, that for $27 billion you get $62 billion worth of asset is certainly not the whole truth, is it?

Mr. BAXTER. The whole truth, Congressman, is you have——

Mr. BACHUS. No, I am asking you.

Mr. BAXTER. I am trying to answer your question. You have insurance policies in the form of a CDS. You have assets that are insured. We got the assets. What happened with AIG is they got to tear up the insurance policy that was threatening its survival.

Mr. BACHUS. Right. I understand all that. I mean, I have heard that repeatedly.

Mr. BAXTER. That is the whole truth.

Mr. BACHUS. But he also says that the fair market value, that you paid the fair market value. But some of these CDOs, some of them they were rated CCC or lower, and the market prices at the time, a lot of them were 20 cents and below that. Is that not correct?

Mr. BAXTER. Well, Congressman, I am a lawyer. I won't comment on the value of any particular asset because it is beyond my competence. In our view and the view of our experts——

Mr. BACHUS. Well, BlackRock, who the Fed hired, they said that they valued the paper at the average of less than 50 cents on the dollar. That would have been somewhat less than $31 billion.

Mr. BAXTER. In November 2008 at one of the worst points in our financial crisis, the loan we made from the Fed to Maiden Lane III, the vehicle that is holding the assets, is a 6-year loan and we have a right of renewal. So we can hold these assets.

Mr. BACHUS. Oh, I understand all that, but I am saying at the time you paid par for something that was trading—BlackRock says they were trading 50 cents on the dollar.

Mr. BAXTER. We paid fair value.

Mr. BACHUS. All right.

Chairman TOWNS. The gentleman's time is expired.

I yield 5 minutes to the gentlewoman from New York, Congresswoman Maloney.

Mrs. MALONEY. Thank you, thank you very much for yielding, Mr. Chairman, and ranking member for holding this hearing.

Along with many of my colleagues, we pushed very hard to have full disclosure and I would like to put in the record letters that I wrote to the Fed requesting full disclosure, along with letters from many of my constituents.

Chairman TOWNS. Without objection, so ordered.

[The information referred to follows:]

Congress of the United States
JOINT ECONOMIC COMMITTEE
(CREATED PURSUANT TO SEC. 5(a) OF PUBLIC LAW 304, 79TH CONGRESS)
Washington, DC 20510–6602

BY ELECTRONIC MAIL AND MAIL DELIVERY

March 4, 2009

Hon. Ben Bernanke
Chairman
Board of Governors of the Federal Reserve

Dear Chairman Bernanke:

As you may recall, late last year, when you were testifying before the House Financial Services Committee, you agreed, in response to my request, to provide me and the Committee with information about the counterparty transactions in which the Federal Reserve (or entities set up and funded by the Federal Reserve) purchased from certain counterparties multi-sector collateralized debt obligations (CDOs) on which AIG had written credit default swap (CDS) contracts. In connection with the purchase of these CDOs, counterparties unwound related CDS transactions. Also, the Federal Reserve funded the purchase of residential mortgage backed securities (RMBS) from AIG. I requested information on the identities of the counterparties from whom the CDOs and CDS were purchased, the price paid by the Fed for the CDOs, CDS and RMBS, and a description of how the prices were determined.

However, to date, your office has not provided that information to me nor, as far as I am aware, to the Financial Services Committee. This letter is to reiterate that request and to ask that the information be provided to me at the Joint Economic Committee and to the Financial Services Committee as soon as possible. As the New York Times editorial said on March 3, 2009 about these very transactions: "The AIG bailouts fail the basic test of transparency: Who ends up with the money?" I agree with the Times that "not knowing is not acceptable."

In further support of my request, I attach a letter from a fellow New Yorker, the noted economist and Nobel laureate Joseph Stiglitz, separately requesting release of this information on his own behalf and explaining how the Fed's providing this information is essential to informed debate over, and efficient development of solutions to, our current economic crisis, as well as to Congress' ability to oversee the use of taxpayers' money with respect to the AIG bailout or similar efforts. This is the letter I put into the record at the Financial Services hearing at which you testified on February 25, 2009.

Thank you very much for your prompt response to this request.

Sincerely,

Carolyn B. Maloney

Carolyn B. Maloney
Chair, Joint Economic Committee

Enclosure

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Joseph E. Stiglitz
University Professor

February 24, 2008

Dear Representative Maloney,

I have been trying to study the impact on the American economy of the bail-outs to AIG and to banks. One of the critical questions is where did the money that we gave them go? It is important to know this for several reasons. First, the claim was made that it was necessary to bail-out AIG in order to prevent systemic risk to the American economy. In order to evaluate this claim, we must know who the ultimate beneficiaries were of the money provided to AIG. If, for instance, the money went abroad, then it was unlikely that AIG's failure would have represented systemic risk to the US. If the money went to a large investment bank, then we can assess the impact on that bank. Perhaps without the bail-out the bank would have survived, though admittedly its shareholders would have been worse off.

Secondly, going forward, we have to devise clear rules about when we will bail-out institutions and when we will not. With our growing national debt, it is imperative that we spend taxpayer dollars wisely. If only a small percentage of the AIG money went to banks which were systemically important, it would have been far more efficient to assist directly those firms. The AIG bail-out provides a good case study within which to frame this important policy debate.

Unfortunately, the public does not seem to have access to this information. I realize that some claims may be made that releasing such information at the time of the bail-out might have exacerbated market turmoil. I am, however, a strong believer in market transparency. Many of our current problems can be traced to inadequate transparency. Whatever one's views on this, sufficient time has elapsed that these concerns are no longer relevant. American taxpayers have a right to know where their money is going, and it is imperative that Congress has this information in order to frame appropriate legislative responses.

Firms should play by the rules. The basic rule of capitalism is that firms should bear the consequences of their mistakes. If there are exceptions, they should be narrow and well defined. I am requesting that you make publicly available information about who received the money given by the Fed and the U.S. Government to AIG and about the derivative contracts under which this money was delivered. The information I am requesting should be of immense help in assisting Congress to undertake the essential analyses I have described.

It would also be useful to know the analyses that the Federal Reserve and Treasury undertook prior to the bail-out, which led them to the conclusion that the failure of AIG would lead to systemic risk, as well as the analyses that they undertook prior to the decision not to bail-out Lehman Brothers which led them to the conclusion that the failure of Lehman Brothers would not lead to systemic consequences. It is important that the government have appropriate analytic frameworks for addressing these questions, and it is apparent that, at least in the case of Lehman Brothers, the existing frameworks are deficient.

As the current crisis continues to grow, it is important to have this information as quickly as possible.

I look forward to your response.

Sincerely,

Joseph E. Stiglitz
University Professor
Columbia University

Mrs. MALONEY. OK. I would like to get back to Mr. Bachus' questioning, Mr. Baxter, where you bought the $62 billion for $29 billion. My question is, what is the value now?

Mr. BAXTER. The value now, I can't say, Congressman.

Mrs. MALONEY. Well, did the taxpayers win or lose?

Mr. BAXTER. Right as of today, we have a situation where our loan balance is $4 billion less than the amount of the portfolio, which I will estimate and I think I need to estimate, our loan balance is around $17 billion and the portfolio is around $21 billion or $22 billion.

Mrs. MALONEY. Well, let's get back to the line of questioning from Mr. Cummings. I know, and we all know that we released the names of the counterparties, but I understand that you still want to withhold other information concerning these assets. And what is that information? And why do you want to continue to keep it a secret?

We believe, in Congress, many of us, that sunshine is the best disinfectant, and anti-corruption and fraud deterrent. So why do you feel this should be kept secret? What is it and why do you feel we want to keep it secret?

Mr. BAXTER. The information that we are still concerned about at the Fed on the schedule A to the shortfall agreement is information about the CUSIP numbers and tranches of the multi-sector CDOs that the Fed now has in Maiden Lane III, its vehicle. Our experts, BlackRock, tell us that if we publish that information, when the day comes, and it may be 4 years, it may be 6 years, it may be longer, when the Fed wants to sell those assets, that we will be hurt. We will be hurt because traders in the market will know what we are holding. Like in a card game, if one player shows his hand to everyone else, that one player is prejudiced.

So that is the worry. The worry is it will injure the taxpayer interest if we show our hand, if we show our CUSIP numbers and our tranches. So that is the key. And we applied for——

Mrs. MALONEY. Well, Mr. Baxter, reclaiming my time, isn't it standard policy for investors to disclose holdings like these in securities filings?

Mr. BAXTER. Well, these particular multi-sector CDOs, it is not customary, I am told, for investors to put this information out. And if you do, again I am relying on what experts at BlackRock have told us, if you do, you can be gamed by hedge funds and sophisticated players when the time comes when you want to sell.

Mrs. MALONEY. So you are saying that the public, the taxpayer would be at greater risk in the ability to reclaim these funds if this information was disclosed. Is that true?

Mr. BAXTER. That is true, Congresswoman. I would also wonder why the average American would need to know the precise CUSIP numbers and tranches of the Maiden Lane portfolio. It is the kind of information that, at least in my household, my family wouldn't know how to interpret. But sophisticated players, hedge funds, traders on the street, they could game us if that information was out there.

Mrs. MALONEY. Going forward, the Financial Services Committee has passed a regulatory reform bill that includes in it resolution authority which would be a wind-down authority so hopefully we would not be in this type of crisis again.

And I would like to ask Mr. Friedman from, you say you weren't privy to this information, but your experience in finance, do you think things would have been different if there was a more formal process for AIG such as this resolution authority? And could you tell us the difference between government or taxpayers bailing out AIG and Lehman, which is a question many of my constituents are perplexed over. What was the difference between the two in response?

Mr. FRIEDMAN. Yes, thank you, Congresswoman.

As I mentioned when you and many of your colleagues were voting, the Board of the Federal Reserve Bank of New York has ring-fenced away from these supervisory regulatory or, and certainly these extraordinary issues. So I have no direct knowledge from that standpoint of this.

So what I am giving you is my opinion just as a person who's been around markets for many years. I do believe that for our financial system to work effectively, we have to get away from too big to fail, too intertwined to fail. I think these are dangerous things, and I earnestly hope that as Congress works its way through restructuring our financial regulatory system, they will have some form of resolution authority to give the people who are on the firing line the next time a crunch comes, and one will come at some point in the future, the ability to effect some sort of a conservatorship or resolution to wind down these entities.

I think that people who are making money in markets should be at risk of losing money. But if there is not the ability to do this without jeopardizing the entire financial system of the country, very much including Main Street, I think people get their hands tied behind their backs. So I earnestly hope we will have some kind of a resolution authority.

As far as the difference between Lehman Brothers and AIG, I have no direct inside knowledge of this. I can say that AIG was a, to an outside observer, much bigger, more complex and even more dangerous to the economy type of a situation, and there may well have been, and this Mr. Baxter would be much better able to answer than I, there may have been very much a difference in terms of the Fed's ability to enter into it based on the quality of the collateral they could get, but that I can't speak to personally myself.

Chairman TOWNS. The gentlewoman's time has expired.

Mrs. MALONEY. Thank you, Mr. Chairman.

Chairman TOWNS. I yield now 5 minutes to the gentleman from Illinois, Congressman Davis.

Mr. DAVIS. Thank you very much, Mr. Chairman, and I thank each of you for being here.

Mr. Friedman, let me ask you, what was the role of the Board of Directors of the Federal Reserve Bank of New York in the decision to compensate AIG counterparties at par?

Mr. FRIEDMAN. Yes, sir, my strong understanding and recollection of our role is that we were in effect an advisory board on most issues, with administrative responsibilities for things like controls, audit committee, etc. And so we were walled away, ring-fenced away from regulatory issues, supervisory issues, or the extraordinary types of emergency interventions that took place during 2008.

If you think of the makeup of the Board, during my tenure something like six of the nine members either had some affiliation with banks or with financial institutions, so there would have been myriad conflicts if we had been involved.

In my experience, the staff of the bank was very meticulous in keeping us involved in these transactions, so I can say that I played no role in any of these decisions or in ratifying them. I have been advised very recently that on the night that the AIG transaction was finalized, I and the chairman of our Audit Committee received a courtesy summary briefing from Fed officials telling us what had happened and that this would be announced the next morning.

So I hope that is responsive.

Mr. DAVIS. Well, let me ask, during the time period in October and November 2008, when the Federal Reserve Board of New York's staff were deciding how to address the problems, how to deal with them, did you get any briefings from the staff on the actions that they were taking and the policy options that they were considering?

Mr. FRIEDMAN. I recollect no such briefings during the period that they were trying to determine what to do. I have no recollection of ever being asked for my views or proffering my views. I have a recollection of, after the September intervention when AIG was carried out, that evening being getting a courtesy summary posting from Mr. Geithner telling us what they had done, which would be in the newspapers the next day. And all of this was consistent with a design, as I understand it, of the statute that a prior Congress passed for how the Federal Reserve Banks should operate.

Mr. DAVIS. You are on the Goldman Sachs Board of Directors?

Mr. FRIEDMAN. Yes, sir.

Mr. DAVIS. And you were on the Goldman Sachs Board of Directors in late 2008?

Mr. FRIEDMAN. Yes, sir.

Mr. DAVIS. As the chairman of the Federal Reserve Board of New York, the Bank Board of New York Board of Directors, do you think your access to information and the decisionmaking process at the Fed gave Goldman Sachs an advantage in weathering the storm when there were so many other firms floundering and folding?

Mr. FRIEDMAN. Sir, absolutely none, because the staff of the Federal Reserve Bank of New York, in my experience, was very careful and meticulous to keep us away from any information that would be of the type of nature you talk about. The potential for conflicts was rife there.

You know, the purpose of that Board, the primary purpose, as I saw it, was it gave the president of the bank a group of knowledgeable market people that he could get information from as to what was happening in their areas, their business areas, and their communities. And I would speculate that if you had a Federal Reserve Bank in an area in the Southwest, you would want oil expertise.

In an agricultural area, you would want people with farm expertise.

We had a lot of financial market expertise, but the discussions were at the level of what are you seeing in the markets, what are you seeing in the economy. They wouldn't ever tell you what was happening in another bank, which was probably a competitor of one you were affiliated with. And I just think it was handled in a very professional and meticulous fashion.

Mr. DAVIS. So the firewalls were there that would prevent any conflict of interest?

Mr. FRIEDMAN. In my experience, they were very carefully supervised, sir, and I never had a sense that anyone had any desire to transgress.

Mr. DAVIS. Thank you very much.

Thank you, Mr. Chairman.

Chairman TOWNS. The gentleman's time is expired.

I now yield myself 5 minutes, but I will yield a minute to the gentleman from Massachusetts before I raise my questions.

Mr. LYNCH. Thank you, Mr. Chairman.

Mr. Friedman, just following up on Mr. Davis' question. I am concerned about the overall influence of Goldman Sachs in Treasury and at the Fed. And I think your own situation is somewhat instructive. As I understand, you were previously on the Goldman Sachs Board of Directors.

Mr. FRIEDMAN. I was. During the period you have been discussing I was and I am still on this.

Mr. LYNCH. Right. OK. And then you became a member of the New York Fed Board of Governors?

Mr. FRIEDMAN. Yes, sir.

Mr. LYNCH. OK. And while you were there, apparently you owned a significant amount of shares in Goldman Sachs, but that was OK at the time because they were not a bank holding company. Right?

Mr. FRIEDMAN. Yes, sir.

Mr. LYNCH. And then when they became a bank holding company, you had a decision to make, and that was to either divest, right? Or get a waiver?

Mr. FRIEDMAN. Yes.

Mr. LYNCH. And you applied for the waiver.

Mr. FRIEDMAN. Well, the Fed staff applied for the waiver. I did not apply for the waiver.

Mr. LYNCH. OK. And then while the waiver was pending, you bought 37,000 more shares of Goldman Sachs.

Mr. FRIEDMAN. Yes.

Mr. LYNCH. What was the thinking behind that?

Mr. FRIEDMAN. Let me tell you what the—when I went on the Fed Board, the Fed Reserve Board, I was a director of Goldman Sachs. I had Goldman Sachs shares and I would be regularly receiving Goldman Sachs shares as part of your directorship grants.

Mr. LYNCH. I get that part, but if you are not in compliance and you are asking for a wavier, what about the decision to buy 37,000 more shares of Goldman Sachs?

Mr. FRIEDMAN. OK. At the time Goldman Sachs became a bank holding company, I then became technically ineligible to be a Class E Director. So there were a number of options.

I was not going to at that point, it would not have been feasible for me to resign from the Goldman Sachs Board and sell all my shares. I had done that several years before when I went to take an administrative post in a prior administration. So that left two options. One was for the Fed to basically say your status has changed; you need to resign, in which case I would have promptly saluted smartly and resigned that afternoon.

Mr. LYNCH. Excuse me, sir. I am sorry, but your answer is, for the last 3 minutes, has been unresponsive. So you knew you were not in compliance. You had to apply for a waiver to stay in that position, yet you bought 37,000 more shares. Can you please, and I don't mean to badger you, but could you answer that part of the question?

Mr. FRIEDMAN. I will. My understanding of the practices and precedents of the Federal Reserve was that during the pendency of a waiver, you continued on in your role as a director and the rules were in abeyance. And that was actually the practice of what happened. I continued chairing the Board. Ultimately during this period, when Mr. Geithner was tapped to go to Washington——

Mr. LYNCH. I still don't understand.

Mr. FRIEDMAN. And I during this period, I made a decision in December to buy some Goldman Sachs shares. This did not change the eligibility at all because——

Mr. LYNCH. You just owned more. Here is the problem, as a member of the Board of Governors, you are making decisions on matters that directly affect Goldman Sachs. And you are a former shareholder, current shareholder, and then you buy 37,000 more shares of that company that you are overseeing.

Mr. FRIEDMAN. Yes.

Mr. LYNCH. Therein lies the problem. Let me ask you, I notice in dealing with Treasury and the Fed that there are a lot of Goldman Sachs employees all over the place here. Is there any type of program where Goldman encourages their employees to sort of salt the regulators' offices that they are regulated by?

Mr. FRIEDMAN. Certainly none whatsoever in the sense of, gee, this is some kind of a firm strategy. That I can tell you.

Mr. LYNCH. Yes.

Mr. FRIEDMAN. What there has been over the years is a certain tradition that you work here, you try to do well for yourself and your family, and then you give back and you do public service. For many years, this was regarded as a very constructive and positive thing.

Mr. LYNCH. I can see that.

Mr. FRIEDMAN. Lately, it has gone the other way and people are thinking is there some ulterior motive.

Chairman TOWNS. Reclaiming my time, reclaiming my time. It was, you know, initially it was a minute, you know.

Mr. LYNCH. Thank you. You have been very generous, Mr. Chairman.

Mr. ISSA. I would ask unanimous consent that the chairman have an additional minute added.

Chairman TOWNS. Thank you very much. I appreciate that.

Let me just say that we are going to close out. But just before we close, Mr. Friedman, let me just ask you. You still sit on the Board of Goldman Sachs. Right?

Mr. FRIEDMAN. Yes, sir.

Chairman TOWNS. The CEO of Goldman Sachs has said that he didn't need the billions he received in counterparty payment from AIG. He said he didn't really need it. If that is the case, why doesn't Goldman Sachs give back the money? Mr. Friedman, my advice to Goldman Sachs is just come clean and say you need the money and you appreciate the fact that the American taxpayers were so generous. Why not?

Mr. FRIEDMAN. You were talking, sir, about a financial transaction where the Goldman Sachs people were in a commercial transaction with AIG.

Chairman TOWNS. That is correct.

Mr. FRIEDMAN. And they had entered into at a time when AIG was a AAA company and they were doing it, acting as intermediaries for Goldman Sachs clients. They had worked very carefully on their risk management to protect themselves against a deterioration in the value of these CDOs or in the deterioration of the value of AIG, and they felt that they were fully hedged and had protected their shareholders' interest.

I do not think that there is any feeling there that they did anything other than what a market participant would do in the normal course.

Chairman TOWNS. You are saying they did not need it. Is that what you are saying?

Mr. FRIEDMAN. Well, what I would say was this. Goldman Sachs has consistently said—there was something like $20 billion, round numbers for illustrative purposes, of instruments that they sought insurance on. There was a deterioration in the value of that. Let's say, illustratively, roughly half. They felt that AIG, from whom they had purchased this credit insurance, owed them $10 billion. They had $7.5 billion of collateral. That left a shortfall of $2.5 billion. They had purchased insurance on AIG's survival from other major institutions and had collateral and netting arrangements with these other institutions.

So what they have consistently said is that their direct exposure, and they have used that word, direct exposure, to AIG was not material.

Now, I am not going to say that, and this may be the point that the SIGTARP made, but I am not going to say that in the event of a financial Armageddon, all bets weren't off, but they are the stewards for the money of their shareholders.

Chairman TOWNS. All right.

Mr. FRIEDMAN. And that is the——

Chairman TOWNS. Thank you very much.

Mr. ISSA. Mr. Chairman, just a couple of quick UCs? I would ask unanimous consent that all Members have 5 legislative days in which to submit both their opening statements, and any followup questions to any of our witnesses.

Chairman TOWNS. Without objection, so ordered.

Mr. ISSA. I ask unanimous consent that the letters earlier submitted, that if the Chair would eliminate his reserve at this time. These are letters that you were copied to a long time ago, hopefully.

Chairman TOWNS. Right. Definitely. Still reserving the right to object because some of them I am not sure I have seen, so I want to make certain that we see them. I don't really see a problem, but just in case there is a problem, I want to reserve the right.

Mr. ISSA. OK. Well, actually, I will withdraw my UC on that and simply submit them as new questions for the record. Perhaps that would be easier.

Chairman TOWNS. Without objection.

Mr. ISSA. And then last, the UC on, or second last, the UC on the schedule A. Are you prepared to withdraw your reservation on that at this time?

Chairman TOWNS. I am prepared to withdraw.

Mr. ISSA. Thank you, Mr. Chairman.

And last, earlier you had said that you would compel witnesses to answer. It is the custom of the committee that it be 7 days. Could I have unanimous consent that 7 days after their receipt, they be expected to respond to our questions?

Chairman TOWNS. Without objection.

Mr. ISSA. Thank you, Mr. Chairman, and thank you for holding this incredibly successful hearing. I think this is probably our finest bipartisan hour. I think the witnesses, whether they liked the questions or not, would certainly agree it was bipartisan.

I yield back.

Chairman TOWNS. Thank you very much.

Let me thank all of our witnesses for being here today, and of course we really appreciate the fact that you have taken the time to come.

And without objection, I enter this binder into the committee record.

But before we adjourn, let me state that if the AIG bailout and the Government's involvement in it teaches us anything, it shows that deals with the taxpayers' dollars that are made in secret results in distrust and deep, deep, deep disappointment. When taxpayers' dollars are involved, transparency must be first and the last focus of the government.

Again, let me thank you very, very much for your testimony.

Mr. BACHUS. Mr. Chairman.

Chairman TOWNS. I yield to the gentleman from Alabama.

Mr. BACHUS. Could I, with your leave, just mention one email in particular that I think highlights what you just said?

Chairman TOWNS. Let me just say to you, put it in writing. He will answer it, and we will move forward.

Thank you very much.

[Whereupon, at 3:22 p.m. the committee was adjourned.]

[The prepared statement of Hon. Gerald E. Connolly and additional information submitted for the hearing record follow:]

Statement of Congressman Gerald E. Connolly

Committee on Oversight and Government Reform

"The Federal Bailout of AIG"

January 27th, 2010

This hearing reminds us, yet again, of the damage caused by unchecked fealty to the barons of Wall Street. Though the severity of the recession and slow recovery has obscured memories of the events that led to the housing market collapse, some may recall that economists warned of risky financial sector activity in 2005, when the bubble was still inflating. Former Federal Reserve Chairman Alan Greenspan dismissed such warnings, claiming that rational market actors could not possibly overvalue housing prices to the extent that we just witnessed. So too certain members of Congress engaged in a deregulatory frenzy, banning regulation of derivatives and repealing successful regulations such as the Glass-Steagall Act, which had been passed in reaction to the Great Depression. Many of them would have us forget all that and accept their specious arguments that somehow Tim Geithner started it all. This is a smokescreen.

As a result of this deregulatory fervor, the financial collapse in the fall of 2008 destroyed over $3 trillion of value in our economy, and the myopia of Wall Street investors led directly to financial hardship for millions of Americans, including the 10% of the population that is currently unemployed. In response to the financial collapse, former President Bush and his appointees, who themselves had worked for the very same Wall Street firms that caused the collapse, wrote a blank check for nearly a trillion dollars to prevent even more firms such as AIG from going broke. That intervention may well have been a necessary evil to prevent further economic contraction. Whether it was necessary or not, there is no question that it would not have been needed if former Congresses and an ideologically driven Federal Reserve had not abandoned the financial regulations that have served America well since the Great Depression.

Under the Bush Administration, former Republican Secretary Paulson and the Federal Reserve Bank arranged for counterparties to AIG to receive 100% of the value of the Credit Default Obligations. It is highly unusual for creditors to a bankrupt company to receive 100% of the money that the bankrupt company owes. It is outrageous that Bush Administration officials and their allies in the Federal Reserve allowed this payment at 100% value. The more important question is why the Treasury and Federal Reserve even had the ability to make counterparty payments that were so generous. The answer, of course, is that former Secretary Paulson and the Federal Reserve were acting under the authority of the TARP plan proposed by the Bush Administration, a blank check from taxpayers to Wall Street. The same officials who deregulated Wall Street readily reimbursed the investors who made bad decisions by purchasing Credit Default Obligations from AIG.

Now, those same individuals are opposed to financial reform, claiming that it will preclude financial sector "innovation." We should all be able to agree that the use of Credit Default Swaps to trade toxic mortgages was very innovative. It was also very destructive. If we are to avoid another financial sector collapse, with its collateral damage on the economy, broad-based reform such as that which passed the House, over the objection of the same minority that brought us this crisis and over a hundred banking lobbyists who assisted it, will be necessary.

Committee on Oversight and Government Reform
Questions for the Record
Hearing: January 27, 2009 - "The Federal Bailout of AIG"

QUESTIONS FOR SECRETARY GEITHNER

By Representative Marcy Kaptur:

1. Mr. Secretary, who nominated you to be President of the Federal Reserve Bank of New York? Please describe in detail the vetting process that you experienced both before and after you were nominated.

2. You stated in your testimony that after your election to be President of the Federal Reserve Bank of New York, you had to receive approval from the Chairman of the Federal Reserve Board of Governors, and that there were many checks and balances in the process. Can you please describe in full the process of approval for you – please include number of meetings, those present at each of the meetings, what was discussed, and include all related documents. I'd like to have a clear understanding the checks and balances in place and to what end these checks and balances work. Please also include a complete timeline of this approval process from start to finish.

3. Since the inception of the Federal Reserve System in 1913, please tell me the number of Presidents of any of the twelve Federal Reserve Banks that were elected by the Board of on of the 12 the Reserve Banks and subsequently did not receive the approval of the Chairman of the Federal Reserve Board of Governors.

4. This question concerns the Federal Reserve and Treasury decisions on the creation of a special purpose vehicle called Madden Lane III that bought the underlying collateral of a portion of AIG's credit default swaps for the claimed purpose of preventing further collateral calls, an easing on AIG's liquidity pressures and a strengthening of the financial system.

   The Special Inspector General for the Troubled Asset Relief Program reported on November 17, 2009 (SIGTARP-10-003) there were payments to AIG Credit Default Swap Counterparties of $27.1 billion (Table 2, page 20).

   Of the 16 banks that were recipients of the payments, 12 were foreign. Of the $27.1 billion in payments, the foreign-based banks received $16.6 billion or 61.2 percent of the funds. Goldman Sachs received $5.6 billion (18.8) percent and the balance (20 percent) went to Merrill Lynch, Wachovia and Bank of America

   A. Did U.S. taxpayers and their government have any legal or contractual obligation to make payments to these AIG Credit Default Swap Counterparties?

B. Did the Federal Reserve or Treasury contact the home governments or central banks of the foreign banks and request their assistance in providing these payments?

C. If demands on these foreign authorities were made, what were their responses?

D. If demands on foreign authorities were not make, why not?

E. Was Congress informed of the decision to make these payments beforehand and if so to whom, how and when?

5. Did anyone advise you that you should recuse yourself when President-elect Obama informed you of his intention to nominate you to be Treasury Secretary? If "yes", provide their names and the date, content and context of their advice and any related documents.

6. Did you seek or receive legal advice or the expert ethical advice as to whether and how you should recuse yourself? If "yes", provide their names and date, content, and context of their advice and any related documents. If "no", why did you not seek such advice?

7. When and how did you advise the Office of Government Ethics (OGE) of your recusal? Provide any related documents.

8. Explain in detail why you recused yourself and the exact nature and language of the activities which you recused yourself from performing. Explain why those activities posed a potential ethical problem absent recusal. Provide all related documents.

9. Who did you appoint in your recusal to perform the duties from which you were recusing yourself? How did you inform them, and the Federal Reserve Bank of New York and the Board of Governors of the Federal Reserve, of your recusal and the appointment of your substitute decision makers? Provide all related documents.

10. When and how did you inform the incoming incoming Obama administration of your recusal? What was their response? Provide all related documents.

11. Why did you fail to recuse yourself in writing? When and how did you become aware of the requirement to confirm any recusal in writing? Provide all related documents.

12. Who did your recusal identify as the official(s) to screen communications in order to make the recusal effective (as required under OGE rules)? OGE takes the position that recusal requires the official to appoint screeners to prevent the recused official of being involved even in communications, not simply decisions, concerning the subjects of the recusal. Did you recuse yourself from any involvement, including the receipt of information, related to the subjects from which you recused yourself? If not, why not? Provide all related documents.

13. When did you first make public your recusal? Did you direct, urge, or imply that your recusal not be made public? Provide full details and all related documents.

14. Do you concede that your recusal procedures failed to comply with the law and best ethical practices?

15. Explain fully and in detail the potential conflicts of interest that could have arisen from your participation in decisions concerning AIG. Provide any related documents.

16. By recusing yourself from regulatory activities in November 2008, during what you describe as a crisis that threatened a second Great Depression, you removed the most senior field regulator of many of the largest bank holding companies at a time when your expertise was most critical. Provide a list of the bank holding companies and state chartered member banks with assets over $1 billion that the Federal Reserve Bank of New York (FRBNY) regulated at the time of your recusal. Why did you believe that the potential conflicts of interest were so severe that they compelled you to recuse yourself during this desperate crisis? Provide any written or electronic explanation of your decision prior to your testimony.

17. Provide in detail, with any related documents, your understanding of the business strategy of each AIG CDS counterparty in its dealings with AIG, the Fed, or any U.S. agency with regard to obtaining full payment on its CDS. Identify and provide all related documents.

18. If the counterparties had forced AIG into bankruptcy, what was AIG's, Treasury's, the Fed's, and the FRBNY's analyses of how large their recovery would have been on the CDS. Provide all such analyses and identify the dates on which they were conducted and who received such analyses. What analyses did you order of how much each counterparty would receive should AIG declare bankruptcy? When did you request or direct such analyses to be conducted? Who prepared them and when did they report their results? What were those results? Identify and provide all related documents.

19. Do you agree that if the counterparties had forced AIG into bankruptcy they were likely to suffer large losses on their CDS? If not, provide a detailed explanation of your rationale. Identify and provide all related documents.

20. Do you agree that the U.S. government had unprecedented leverage with regard to the AIG CDS counterparties given the government bailout of AIG and many of the AIG counterparties? If not, provide a detailed explanation of your rationale?

21. Describe in detail your analysis of how the U.S. government could have best used its leverage to avoid paying roughly 100 cents on the dollar for the CDS had that been your mission. Identify and provide all related documents.

22. Why didn't the U.S. use its roughly 80 percent ownership of AIG to spin off AIG's trading arm and place it in bankruptcy? Describe in detail the U.S. government (including the FRBNY and the Fed) and AIG research into its bankruptcy options for AIG. Identify and provide any advice, including legal advice, that the U.S. government or AIG received concerning such a potential spin off and bankruptcy filing by the trading arm.

23. Did the U.S. government (including the Fed and the FRBNY) take any action to demand that the AIG CDS counterparties cease demands that AIG post additional collateral? If not, why not? If they did, describe the efforts (and the response of the counterparties) fully. Identify and provide all related documents.

24. What monitoring of AIG's exposure to CDS written on CDOs did NY Fed undertake in
    a. 2004-2006
    b. H1 2007 after HSBC mortgage blowup
    c. H2 2007 after Bear Stearn Hedge Fund blowup
    d. Q1 2008 after monoline distress
    e. Q2 2008 after Bear blowup and acute monoline distress
    f. Q3 2008 in run up to collateral calls on AIG?

    subject to result of above questions). The following blog entry, by an anonymous securities lawyer familiar with the terrain, criticises a financial journalist for obliviousness to the level of risk at AIG in mid-2007, pointing to a widely distributed Fitch report that highlight's AIG's exposure. AIG was well known as a major, if not the major, credit default swaps counterparty. Certainly by the time of the Bear Stearns rescue, if not sooner, credit default swaps were recognized as a source of systemic risk; if nothing else, Eric Dinallo of New York State Deptment of Insurance made that clear in January 2008. Why was there no interest in AIG as a source of counterparty risk to the dealer community? http://economicsofcontempt.blogspot.com/2009/09/risk-held-at-aigfp-was-not-surprise.html

25. On what date did Treasury start making contingency plans for a run on AIG? What the NYFRB involved?

26. On what date did Treasury begin liaison with AIGFP's regulator UK's FSA? What the NYFRB involved?

27. On what date did Treasury start the process of discovering who AIG's counterparties were for the CDS's written on CDO's by AIG? What the NYFRB involved?

28. What risk modeling or other assessments did Treasury undertake of the resulting systemic risk and when did they start? What the NYFRB involved?

29. What legal advice did Treasury take regarding the prospect of successfully challenging the French claim that settling the AIG CDS on CDOs for 100 cents on the dollar would be illegal under Franch law?

30. Is it correct that you claimed at the time that legal obstacles faced by the French banks were a major reason why haircuts could not be negotiated?

31. Are you aware that it has since become clear that those legal difficulties were fictitious?

32. Considering how Socgen and Calyon were both very closely linked to US banks in particular, over half of SocGen's exposure was underwritten by Goldman, for example], is it possible that US banks knew about or encouraged French banks to urge their regulators to represent their legal situation falsely? Do you think an investigation might be warranted?

33. Some of the owners of the CDOs purchase by Maiden Lane III were not the banks, but their clients. They are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance? Who were the third party clients of Goldman (and others?) who benefited from the Maiden Lane III payments to Goldman? Was any investigation performed to determine who they were and whether they were appropriate recipients of taxpayer payments? Were any conflicts of interest investigated with respect to such payments?

34. Why did you as President of the Federal Reserve Bank of New York not work out an arrangement to remove the AIGFP until from the company and dealing with it separately rather than allow the AIGFP unit to infect the entire company?

35. The AIG transaction was disturbing to many observers. Why did out government not require the bank creditors to take the lead and bear the loss in our plan to stabilize AIG? You in effect nationalized the company and let the creditors off the hook?

36. What's the propriety of the taxpayers, via our subsidy to AIG, paying UBS $5 billion while the Justice Department was prosecuting it for massive tax fraud?

37. In the hearing did you say that losses to the banks would not have been material had AIG not paid 100 cents on the dollar – that makes paying 100 cents on the dollar insane? Any reasonable party could have negotiated a better deal. Other financial troubled entities paid 13 cents on the dollar for their CDS's.

38. Mr. Secretary, in your previous position, what did you do during the negotiations with AIG's counterparties to get the counterparties to accept less than 100 cents on the dollar, if anything? Were you working to make whole the Wall Street member banks, the Federal Reserve System, the American people, or none of the above?

39. The CEO of Goldman Sachs was asked at the Financial Crisis Inquiry Commission if the government had asked Goldman to participate in the rescue of AIG. He responded "Not to my knowledge." In hindsight, what would you change at of the AIG transactions? Was there a better way to calm the markets without doing so much damage to the company and destroying so much value?

40. Why did the U.S. government limit its role ot facilitate a sector solution rather than destroying the entire company by nationalizing it?

41. Mr. Geither, according your phone log, Congressman Rahm Emanuel 3:30 pm Sept. 16What events were transpiring related to crisis at that point? What had happened previously? What was the nature of that call?

42. You next spoke to Congressman Emanuel at 10:05 on Sept. 22 sandwiched in between Mr. Mack at 7:27, Mr. Blankfein at 7:56, Chairman Bernanke at 8:00, Secretary Paulson at 8:19, Mr. Pandit at 8:25, Mr. Dimon at 8:32, Secretary Paulson at 9:39, Hector Sants at 9:47, Rahm Emanuel at 10:05, Bob Rubin at 10:10, Alan Greenspan at 11:09, and Rubin again @ 12.57. That seems like an important day. Why Emmanuel and not Pelosi?

43. Next is Sept. 24, sandwiched in between Mr. Rubin at 8:12, Mr. Summers at 8:35, Congressman Emanuel at 10:26, Mr. Altman at 10:56, Secretary Paulson at12:22, and again Mr. Rubin at 12:47. What was the nature of these calls and why Congressman Emanuel and not other Members in Congressional Leadership positions?

44. Why did you not get involved in the negotiations to seek concessions from the counterparties?

QUESTIONS FOR SECRETARY GEITHNER

By Ranking Member Issa:

1. Were you aware that the FRBNY, starting on September 19, 2008, required AIG to submit all "SEC filings, press releases, and other significant communications" to its counsel, Davis Polk & Wardwell ("Davis Polk"), for edits and approval?[1] If you were aware of this policy, did you approve it? If you were unaware of this policy at the time, do you now believe that it was appropriate? If you had known that your staff would insist on restricting AIG's disclosures, would you have made sure that AIG was given more autonomy?

2. If an SEC filing by AIG on or after September 19, 2008, had violated the securities laws, should AIG have been able to avoid liability by demonstrating that all of its SEC filings were subject to review, editing, and approval by the FRBNY and its counsel? Would you have agreed or disagreed with your FRBNY General Counsel, Thomas Baxter, when he suggested that AIG could avoid liability for statements made at the direction of the FRBNY?[2]

3. Were you aware that the FRBNY, as of November 11, 2008, did not want to disclose that AIG's CDS counterparties were going to receive the par value of the underlying assets in the Maiden Lane III transactions?[3] Did you order your staff not to disclose this fact? If you were unaware that the FRBNY did not want to disclose this fact, do you now believe this non-disclosure was appropriate?

4. Were you aware that the FRBNY specifically ordered AIG not to disclose, in its SEC filings, that its counterparties received par value?[4] Did you approve this order? Were you aware that Davis Polk did, in fact, delete a sentence containing such a statement from one of AIG's SEC filings?[5] Do you now believe that it was appropriate for the FRBNY to order AIG not to disclose in its SEC filings that its counterparties received par value? If a member of the FRBNY legal staff had requested your approval to direct AIG to remove such statements from its SEC filings or from other communications, would you have approved?

5. When did you first become aware that members of Congress wanted to know the names of AIG's counterparties?[6] Was it appropriate for the FRBNY to resist the

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[1] *See* FRBNY-TOWNS-R3-002263-64.
[2] *See* FRBNY-TOWNS-R1-039070 ("If someone sues AIG, they can say the Fed told us to do it").
[3] *See* FRBNY-TOWNS-R1-191773.
[4] *See* FRBNY-TOWNS-R1-005137.
[5] AIGHOGRM2200 (deletion of the following sentence from AIG's Form 8-K, filed Dec. 24, 2008: "As a result of this transaction, the AIGFP counterparties received 100 percent of the par value of the Multi-Sector CDOs sold and the related CDS have been terminated").
[6] *See* FRBNY-TOWNS-R1-139505 (Fed Congressional Liaison reports to FRBNY staff members on a Nov. 10, 2008 phone call with staff of the Senate Finance Committee and relays questions about the identities of AIG's counterparties).

disclosure of the names of AIG's counterparties to Congress?[7] Was it appropriate for the FRBNY to resist the disclosure of the names of AIG's counterparties to the public?

6. Do you agree with FRBNY staff's request to the SEC that AIG's list of the assets Maiden Lane III had acquired, with counterparty names, transaction amounts, and securities identifiers, be treated in the same manner as "national security related files"?[8] If so, why was the information contained in the document so sensitive?

7. Was it appropriate for the FRBNY to contact the SEC directly to argue that a portion of AIG's filings should be kept confidential and should not even be submitted to the SEC as part of its confidentiality determination? Or should the FRBNY have allowed AIG to conduct all communication with the SEC regarding its filings on its own?

8. On March 16, 2009, AIG released selected information from Schedule A to the Shortfall Agreement between AIG and Maiden Lane III, including the names of its counterparties and aggregate pricing information for the purchases of underlying assets from the counterparties. Federal Reserve officials had warned that these disclosures would "undermine AIG's stability, the privacy and business interests of the counterparties, and the stability of the markets."[9] Do you agree that these warnings were wrong and that AIG's stability, the counterparties' interests, and the markets' stability were unaffected? Or do you believe that adverse consequences followed from AIG's March 16, 2009 disclosures?

9. On January 27, 2010, the Committee on Oversight and Government Reform released the remaining information from Schedule A, including identifying information for each underlying asset that Maiden Lane III purchased from AIG's counterparties and the notional value, collateral posted, and negative mark-to-market associated with each individual transaction. What adverse consequences, if any, do you believe have resulted, or will result, from this disclosure?

10. On October 15, 2008, Sarah Dahlgren, an FRBNY Vice President, wrote you an e-mail message, reporting that "Board staff again reiterated that they didn't think that the Governors (unnamed) would go for ML2 or ML 3...they continue to push back hard on ML 3."[10] What was the conflict between your staff at the FRBNY and the Federal Reserve Board staff in Washington regarding the planned

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[7] *See, e.g.*, FRBNY-TOWNS-R3-008604 ("Congress has enough information to assess what we did right now. They just want the counterparty names for purposes of political illustration...."); FRBNY-TOWNS-R3-011119 (FRBNY staff member speculates on the SEC's treatment of a filing by AIG: "Finally, even if we succeed in redacting the stuff we want to redact...this redacted information will still sit in the SEC's files, and the SEC may well get a request from Congress for that information. I don't know if there's a way to manage it so that Congress won't ask for it, or if they do, won't release it").

[8] *See* FRBNY-TOWNS-R3-004119.

[9] Office of the Special Inspector General for the Troubled Asset Relief Program, *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Nov. 17, 2009, at 31.

[10] FRBNY-TOWNS-R1-205129.

establishment and transactions of Maiden Lane III? Why did the Federal Reserve Board eventually agree to go ahead with Maiden Lane III?

11. On November 17, 2008, AIG submitted a draft SEC filing to the New York Fed and Davis Polk for review, edits, and approval. The filing reported that a new compensation package had been signed by AIG's CFO, David Herzog. Within 40 minutes, Marshall Huebner, the lead partner for Davis Polk's FRBNY business, sent an e-mail titled "READ ME" to Thomas Baxter, the FRBNY General Counsel. Huebner wrote, "Very bad timing to have this 8k come out just before the Secretary and the Chairman go before Waxman…Is there any chance—and maybe it is just too late—to get the Herzog comp package unagreed to?"[11] AIG never filed the SEC filing, and evidently canceled Herzog's compensation package. Were you consulted or informed about the FRBNY's actions in pressuring AIG to cancel the compensation package and not file the SEC filing? Did you approve these actions? If you were not consulted or informed, do you believe the FRBNY's actions in this matter were appropriate? Do you think avoiding embarrassment to the Fed and Treasury was a valid reason to cancel a required SEC filing?

12. Do you believe that it is ever appropriate for the Fed, or Treasury, to force a public corporation that has received extraordinary federal financial assistance to make changes to its compensation arrangements, or take other actions, in order to avoid making disclosures under the securities laws? When are such actions appropriate?

13. AIG and the New York Fed created Maiden Lane III on November 25, 2008. Sarah Dahlgren, a Senior Vice President at the New York Fed in charge of the New York Fed's dealings with AIG, told Davis Polk that she did not want AIG to report the transactions to the SEC that day, saying in an email that "I really don't want the ML III to go out today…is the company still aiming to try to issue this today?..." Ethan James, a Davis Polk partner, responded to her email saying "we gotcha covered. You only need hear Kathy's pathetic vmail to understand how well trained she is-at least for now!"[12] Is it appropriate for a federal government agency to browbeat and control a financial disclosure officer of a public company to the point where she is "well trained?" Is it appropriate for the federal government to dictate the timing of a public company's securities filings solely for its own convenience?

14. One failure of the financial regulatory system that led to the current recession was the inability of the various regulatory entities to effectively share information. In addition, there seems to have been a lack of predictive analysis to identify weaknesses before they became failures. How are the Treasury Department and other regulatory agencies, such as OCC and FDIC, working proactively to

[11] FRBNY-TOWNS-R3-002270

[12] FRBNY-TOWNS-R1-030952.

improve coordination with each other – or even between the divisions of the individual agencies themselves – and what improvements in predictive analysis have been made so that there is an ability to provide the holistic view necessary to prevent future economic crises?

By Mr. Burton:

1. During your tenure as President of the Federal Reserve Bank of New York, to what degree were you involved in the negotiations with AIG's counterparties to determine the price that would be paid for the underlying assets?

2. After the Federal Reserve Board authorized the Federal Reserve Bank of New York to lend up to $85 billion to AIG to enable AIG to avoid bankruptcy, how much of your time was consumed by AIG-related matters?

3. You have stated that you were not a party to the discussions regarding AIG's filings with the Securities and Exchange Commission as those discussions occurred after your nomination to be U.S. Treasury Secretary and you had recused yourself from all Federal Reserve business. You were officially announced as the President-Elect's nominee on November 25, 2008. One of the e-mails subpoenaed by the Committee, dated November 11, 2008, quotes a Federal Reserve Bank official: "As a matter of course, we do not want to disclose that the concession is at par unless absolutely necessary."[13]

    a. Since this e-mail was sent a full 14 days before your nomination as Treasury Secretary is it still your contention that you were completely unaware of any discussion between the Federal Reserve Bank of New York and AIG to hide the details of the AIG counterparties' deal from the American public?

    b. Can you produce a copy of your notice of recusal for the record?

    c. As a key figure in the scenario, and as the potential future Treasury Secretary, even if you were not a party to the discussion, why didn't you insist that you be fully informed on all matters related to AIG's bailout?

    d. If you were excluded from the day-to-day operations of the Federal Reserve Bank of New York during the time period, who was making decisions to conceal information from the taxpayers about how their money was being mis-spent, and when will they be held accountable?

4. Since the beginning of 2009, the Obama Administration has exercised an unprecedented amount of control over the American automotive industry. Some believe this control has resulted in the picking of winners and losers among those retirees who have been impacted by auto bankruptcies. A review of the Master

[13] *See* FRBNY-TOWNS-R1-191773.

Disposition Agreement General Motors filed with the bankruptcy court Southern District of New York clearly indicates that "any GM contributions under a PBGC Agreement will be subject to U.S. Treasury consent."

a. What role did the Treasury Department play in the decision to terminate the pension plan of the Delphi Salaried workers?

b. Did the Treasury Department participate in discussions with the Pension Benefit Guaranty Corporation about the termination of Delphi Salaried workers' pension plan?

   i. If so, what was the position of the Treasury Department in those discussions and the reasoning behind any decision to force only the Delphi Salaried workers to undergo substantial cuts in their pensions?

   ii. Is the Treasury Department willing to publicly release all records and communications between the U.S. Department of Treasury and the President's Automotive Task Force, the United Auto Workers, the Pension Benefit Guaranty Corporation, General Motors, Delphi Corporation and Holding, and any Member of Congress or other public official, referring or relating to retirement or pension benefits for General Motors or Delphi Corporation employees, between November 1, 2008, and November 1, 2009?

5. The United Auto Workers, which represents Delphi Hourly Retirees, has stated that Delphi Salaried Retirees should be treated with fairness and equity. In other words, the UAW supports providing the same "top-ups" to the Salaried workers that were provided to the other Delphi workers. Does the Administration agree?

   a. If so, what steps is the Administration taking or planning to take as the majority owner of General Motors to implement "top-ups" for the Salaried workers?

   b. If not, what is the Administration's justification for continuing to treat these two groups differently?

6. During the hearing I briefly touched upon the question of Representative Ron Paul's "Federal Reserve Transparency Act of 2009" (H.R. 1207), which requires a General Accountability Office audit of the Board of Governors of the Federal Reserve System and the Federal Reserve banks before the end of 2010. The bill is current co-sponsored by 317 Members of the House of Representatives, significantly more than 2/3rds of the total membership of the House. Does the Administration support this legislation to bring more transparency to the operations of the Federal Reserve?

a. If so, is the Administration prepared to work with House and Senate Leadership to schedule a vote on this legislation before the congressional recess in April?

b. If not, why?

7. I have spoken to a number of financial managers about the President's financial reform proposal, and they understandably expressed some serious concerns. So far as I am aware, hedge funds, private equity and proprietary trading were not root causes of the current economic crisis. Can you clarify how the President's proposal would do anything other than limit the competitiveness of American financial companies, particularly in light of the fact that most governments, particularly European governments, have signaled that they are unwilling to pursue similar regulatory reforms?

8. A key lesson that should be learned from the current economic crisis is that companies should be overseen based on the activity they engage in rather than allowing them to choose who they want to be regulated by. Yet, the Administration's proposal seems to create a system that picks and chooses financial companies that will be allowed to drop their status as bank holding companies in order to avoid regulations that would be imposed on other parts of the industry. This seems like a glaring loophole and a fundamental flaw in the President's proposal that would encourage regulatory arbitrage. Do you agree that this loophole exists? If so, are you concerned about its effects and have you thought of ways to fix it?

9. I understand that you have concerns about the President's proposal. Can you elaborate on those concerns?

By Mr. Souder:

1. In its negotiations with AIG's counterparties, why did the FRBNY elect not to factor in the substantial differences in the financial position of the respective counterparties, including their exposure to AIG securities, benefits they may have received from other government programs such as TARP, and the fact that some of the institutions were foreign owned? If you were not directly involved with this decision, do you agree with this policy choice? Did the decision to treat all counterparties the same essentially eliminate any possibility to negotiate concessions?

By Mr. Turner:

1. The administrative record produced by the Pension Benefit Guaranty Corporation ("PBGC") indicates that PBGC staff discussed the Delphi pension plans with officials from the Treasury Department and the Auto Task Force before the plan

was finalized to cut the pension plans. At what date did the Treasury Department know about the cuts to the Delphi pension plans?

2. In what manner was the Treasury informed about the cuts to the Delphi Salaried Retiree pension plans?

3. Does the Treasury Department acknowledge that they knew about the Delphi Salaried Retiree pension cuts prior to final administrative action from PBGC to implement any cuts to those pensions?

4. With what frequency did these discussions occur, and at what level?

5. Did the Treasury Department initiate the discussions with the PBGC regarding the Delphi Salaried Pension plans?

6. Is the Treasury Department consulted in PBGC pension fund plan settlement negotiations?

7. Did the Treasury Department authorize, approve, or consent to the PBGC terminating the Delphi Salaried workers pension plans?

8. Does the Treasury Department deny it had the authority to disapprove of the cuts to the Delphi Salaried Retiree pension plans?

9. What authority does the Department of the Treasury have to prevent the cuts to the Delphi Salaried Retiree pension plans?

10. In the discourse between the Treasury, the PBGC and any other parties, what role did the Treasury Department play in the decision to terminate the pension plan of the Delphi Salaried workers?

11. What was the position of the Treasury Department in any of those discussions and the reasoning behind any decision to force only the Delphi Salaried workers to undergo substantial cuts in their pensions?

12. Recently, it was decided that certain hourly retirees and other union workers whose pensions were cut by the PBGC would have those pensions "topped-up" by the new GM. What role did the Treasury Department have in that decision?

13. How much is the "topping-up" costing New GM?

14. The Secretary of the Treasury sits as one of three board members of the PBGC. Did the Secretary of the Treasury take any action to prevent the cuts to the Delphi Salaried Retiree pension plans?

15. The Secretary of the Treasury sits as one of three board members of the PBGC. Did the Secretary affirmatively consent and/or approve of cuts to the Delphi Salaried Retiree pension plans?

16. The Secretary of the Treasury sits as one of three board members of the PBGC. Why did the Secretary not exercise any authority to prevent the cuts to the Delphi Salaried Retiree pension plans?

17. Did the PBGC vote on the cuts to these plans, and what was the Treasury Secretary's vote?

18. The Secretary of the Treasury sits as one of three PBGC board members. What does the Secretary see as his responsibilities to the PBGC as a board member?

19. Please describe the actual conflicts and potential conflicts between the Secretary's duties as a PBGC board member and the Treasury Department's duties as the majority owner of New GM?

20. How does the Secretary prevent conflicts between those two roles?

21. After the Treasury Department's increased involvement in General Motor's operations, General Motors seemed to reverse its position with respect to assuming the obligations of Delphi's pension plan for salaried workers. Please describe the role of the Treasury Department in that decision?

22. Please provide and describe any communications between the Treasury Department and General Motors with respect to General Motors' position of assuming the obligations of Delphi's pension plan for salaried workers.

23. By the time the PBGC initiated termination proceedings against Delphi's pension plans, the PBGC held approximately $200 million in liens against Delphi foreign assets, and estimated that there were approximately $2.4 billion in Delphi foreign assets that the PBGC could potentially assert liens against. The PBGC ultimately released these liens as part of settlement agreements with New GM and Delphi, in exchange for payments by New GM which did not include Delphi Salaried Retirees pension plans. What role did the Treasury Department play in approving and/or crafting this settlement?

24. When did the Treasury Department become aware that the PBGC believed that there were $2.4 billion in foreign Delphi assets upon which the PBGC could assert liens?

25. Had the PBGC refused to remove the liens, would the Treasury Department have been willing to permit New GM to assume sponsorship of the Salaried pension plan?

26. Did the Treasury Department (or the Auto Task Force) take part in negotiations with the PBGC in an attempt to have the PBGC release its liens against Delphi Assets? And in what manner?

27. When the Treasury Department communicated with the PBGC regarding the negotiation of a settlement agreement and the release of the PBGC's liens, did the Treasury Department take any measures to ensure that the PBGC would not give undue weight to the negotiation position of GM and/or the Treasury Department due to political considerations?

28. Salaried Delphi retirees have made requests under the Freedom of Information Act to the Treasury Department and the Auto Task Force, respectively, regarding their involvement in the termination of the Salaried pension plan. These requests have so far been ignored. Can you explain why the Treasury Department and Auto Task Force have refused to comply with these requests?

29. Members of the House Oversight and Government Reform Committee, as well as other House Members, have requested documentation related to the Treasury Department's knowledge and role in the cuts to the Delphi Salaried Retiree pension plans. These requests have so far been ignored. Please explain the Department's reasoning behind ignoring Congressional requests for information, and please describe when the Department will provide the requested information to the Members of Congress.

30. The United Auto Workers has recently stated that Delphi Salaried Retirees should be treated with "fairness and equity". Additionally, the UAW stated in a letter dated January 15, 2010 that it supports providing the same "top-ups" to the Salaried workers as a matter of "fairness and equity" that were provided to the other Delphi workers. Does the Administration agree?

By Mr. Westmoreland:

1. Once the Government took over 79% of AIG, it was Government-owned. Why did the FRBNY not insist that the Government's Triple-A rating be extended to AIG to ease AIG's collateral posting obligations under its CDS contracts?

2. It is obvious that the AIG deal is bad for taxpayers and that if the deal is not renegotiated taxpayers will never see their money get repaid. Is there anybody at Treasury working on a new plan to deal with AIG?

By Mr. McHenry:

1. In a hearing before the Financial Services Committee last year, you said: "Financial products and institutions should be regulated for the economic function they provide and the risks they present, not the legal form they take. We can't

allow institutions to cherry pick among competing regulators and ship risk to where it faces the lowest standards and weakest constraints." You suggested that you could "reconcile" this view with current financial regulation proposals, which would allow some companies to avoid regulation by dropping their status as a bank holding company. Please explain.

2. Please elaborate on President Obama's proposed tax on banks. Do you believe it will result in less credit being made available to small businesses and consumers?

3. How do you think proposed limits on hedge funds, private equity, and proprietary trading will impact U.S. firms' global competitiveness?

By Mr. Jordan:

1. Do you believe that the management team that the FRBNY put in place at AIG was qualified to run an insurance company? Please describe the relevant experience and qualifications of each FRBNY employee who was given any AIG management responsibilities on or after September 18, 2008.

2. In an e-mail to you on October 22, 2008, Meg McConnell, a FRBNY economist, noted that "the new ML 3-in which they tear up the CDS and purchase the underlying CDOs-seems pretty good from a financial stability perspective...[because] it seems to remove considerably more uncertainty for the firms and arguably for the system."[14] Did the FRBNY consider the finnaical health, or stability, of AIG's counterparties in deciding how to structure and conduct the Maiden Lane III transactions?

3. Do you agree with FRBNY staff's position that a "governmental interest" justified special treatment by the SEC for AIG's filings, distinct from the filings of all other companies?[15] If so, please describe that "governmental interest." Is the "governmental interest" distinct from the policy goals of the securities disclosure laws and rules?

[14] FRBNY-TOWNS-R1-195645.

[15] *See* FRBNY-TOWNS-R3-009189.

By Mr. Luetkemeyer:

1. Why did the FRBNY reject less costly alternatives to acquiring the underlying assets from AIG's counterparties and seeing that they received the full $62 billion up front, such as stepping in to provide collateral to the counterparties as needed under the CDS contracts? If you felt that you did not have the necessary statutory authority, why did you not come to Congress and ask for it?

2. FRBNY General Counsel Thomas Baxter, when asked about the FRBNY's negotiations with AIG's counterparties, told Committee staff, "I don't know why we even bothered to ask [for any concessions]." When he was asked why, he responded, "I guess it doesn't hurt to ask." Why was such a limited effort made to seek concessions from the counterparties?

3. In 2008 and 2009, the FRBNY and its counsel shared AIG's draft SEC filings with officials at Treasury and requested comments and edits. When a corporation's securities disclosures become a group project of multiple federal agencies, with each agency adding changes to suit its own needs, is there a danger that investors' needs will be ignored?

4. You have repeatedly claimed that the Fed will actually make a profit from the AIG bailout. Can you provide any concrete proof of your claims?

By Mr. Stearns, participating by unanimous consent of the Committee:

1. It was brought out in your testimony and through the questions that were asked by the Members of the House Oversight and Government Reform Committee at the January 27th hearing that you did not sign an official, formal agreement to recuse yourself from the dealings and decisions involving the overpayments to AIG's counterparties and from working on issues involving specific companies, including AIG. Because you only informally recused yourself, American taxpayers and Congress have to trust you and take you at your word that you did not get involved with "issues involving specific companies, including AIG" following your nomination for Treasury Secretary on November 24, 2008. Is that true? Please respond with either "yes" or "no".

2. What was the rationale behind your decision to only informally recues yourself? Why did you not sign an official recusal or get an ethical review from the Treasury Department and/or the Office of Government Ethics?

3. You also stated at the hearing that while you recused yourself from the activities dealing with the negotiations over AIG's counterparty payments, you did leave your Chief of Staff in charge to deal with AIG. Is that correct? If not, did your Chief of Staff have any knowledge of the AIG counterparty payments?

4. Is your current Chief of Staff a former employee of Goldman Sachs?

5. Was your former Chief of Staff, while you were President of the FRBNY, a former employee of Goldman Sachs?

6. How can you assure American taxpayers that your Chiefs of Staff always acted in the best interest of the taxpayers and not of Goldman Sachs? What assurances can you give us?

7. Do you believe that without the counterparty payments being made to AIG – at par value – that AIG would have been pushed into bankruptcy and a revolution would have resulted in this country? You inferred this during your testimony, but please clarify this for the record.

By Mr. Blunt, participating by unanimous consent of the Committee:

1. We now know that several of AIG's counterparties were experiencing significant financial difficulties at the time of the decision to purchase the counterparty contracts. How much was the health of these banks a factor in paying them 100 cents on the dollar for the value of their credit default swap contracts?

2. Did the Federal Reserve Bank of New York's decision to treat all counterparties equally give the major counterparties (including foreign banks) effective veto power over the possibility of a concession from any other major parties?

3. What was the extent of the negotiations over paying the counterparties at par value, and what will these same parties do in future times of crisis if Congress enacts legislation to mandate the creation of a $200 billion bailout fund?

4. What was the rationale for keeping secret the list of par value counterparties, given that the SIGTARP concludes that "there is no indication that AIG's disclosure undermined the stability of AIG or the market or damage legitimate interests of the counterparties"?

QUESTIONS FOR MR. HENRY PAULSON

By Representative Marcy Kaptur:

1. Who did you work for what position did you hold before being appointed by President Bush to serve as Secretary of the Treasury?

2. To your knowledge, did any relative of President Bush ever work at Goldman Sachs while you were Secretary of the Treasury, and if so, who and in what capacity?

3. To your knowledge, did any one serving in the White House ever work at ever work at Goldman Sachs while you were Secretary of the Treasury, and if so, who and in what capacity?

4. When you were Secretary of the Treasury, how many people worked in the Department of Treasury who had worked at Goldman Sachs?

5. In the phone logs of Secretary Geithner from Sept. 14 to Dec.31, 2008, when he was President of the Federal Reserve Bank of New York, it shows that he called you well over 200 times. How many of those conversations were about AIG, and when?

6. Why did you use Goldman Sachs to give the Treasury advice on AIG given that Goldman Sachs had a major conflict of interest as a counter party to AIG through CDS's?

7. What monitoring of AIG's exposure to CDS written on CDOs did NY Fed undertake in
    a. 2004-2006
    b. H1 2007 after HSBC mortgage blowup
    c. H2 2007 after Bear Stearn Hedge Fund blowup
    d. Q1 2008 after monoline distress
    e. Q2 2008 after Bear blowup and acute monoline distress
    f. Q3 2008 in run up to collateral calls on AIG?

    (subject to result of above questions). The following blog entry, by an anonymous securities lawyer familiar with the terrain, criticises a financial journalist for obliviousness to the level of risk at AIG in mid-2007, pointing to a widely distributed Fitch report that highlight's AIG's exposure. AIG was well known as a major, if not the major, credit default swaps counterparty. Certainly by the time of the Bear Stearns rescue, if not sooner, credit default swaps were recognized as a source of systemic risk; if nothing else, Eric Dinallo of New York State Deptment of Insurance made that clear in January 2008. Why was there no interest in AIG as a source of counterparty risk to the dealer community? http://economicsofcontempt.blogspot.com/2009/09/risk-held-at-aigfp-was-not-surprise.html

8. On what date did Treasury start making contingency plans for a run on AIG? What the NYFRB involved?

9. On what date did Treasury begin liaison with AIGFP's regulator UK's FSA? What the NYFRB involved?

10. On what date did Treasury start the process of discovering who AIG's counterparties were for the CDS's written on CDO's by AIG? What the NYFRB involved?

11. What risk modeling or other assessments did Treasury undertake of the resulting systemic risk and when did they start? What the NYFRB involved?

12. What legal advice did Treasury take regarding the prospect of successfully challenging the French claim that settling the AIG CDS on CDOs for 100 cents on the dollar would be illegal under Franch law?

13. Is it correct that you claimed at the time that legal obstacles faced by the French banks were a major reason why haircuts could not be negotiated?

14. Are you aware that it has since become clear that those legal difficulties were fictitious?

15. Considering how Socgen and Calyon were both very closely linked to US banks in particular, over half of SocGen's exposure was underwritten by Goldman, for example], is it possible that US banks knew about or encouraged French banks to urge their regulators to represent their legal situation falsely? Do you think an investigation might be warranted?

16. Some of the owners of the CDOs purchase by Maiden Lane III were not the banks, but their clients. They are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance? Who were the third party clients of Goldman (and others?) who benefited from the Maiden Lane III payments to Goldman? Was any investigation performed to determine who they were and whether they were appropriate recipients of taxpayer payments? Were any conflicts of interest investigated with respect to such payments?

17. What's the propriety of the taxpayers, via our subsidy to AIG, paying UBS $5 billion while the Justice Department was prosecuting it for massive tax fraud?

18. What's the propriety of the taxpayers, via our subsidy to AIG, paying UBS $5 billion while the Justice Department was prosecuting it for massive tax fraud?

19. As the Secretary of the Treasury, what, if any power did you have over the Federal Reserve Bank of New York and its Wall Street members?

20. Mr. Paulson, the Oversight and Government Reform Committee has obtained a document from you as Secretary of the Treasury to then President of the Federal Reserve Bank of New York President, Mr. Geithner dated October 8, 2008. In the letter you state that you believed that the Federal Reserve Bank of New York's provision of a special liquidity facility to AIG

in order to allow the company to meet its obligations was necessary to prevent the substantial disruption of to financial markets and the economy that could well have occurred from a disorderly wind-down of AIG.

Mr. Paulson – I assume that these are the Maiden Lane facilities and that these facilities allowed the counterparties to be paid in full. Is that correct?

As the Secretary of the Treasury, what, if any power did you have over the Federal Reserve Bank of New York and its Wall Street members?

QUESTIONS FOR SECRETARY PAULSON

By Mr. Souder:

1. Please explicitly define how you measure systemic risk.

QUESTIONS FOR MR. BAROFSKY

By Ranking Member Bachus, Committee on Financial Services, participating by unanimous consent of the Committee:

1. In preparing your November 2009 Audit of the AIG counterparty payments, were you aware of the November 5, 2008 BlackRock presentation that was widely reported in the media on January 26, 2009, which clearly showed that Goldman Sachs was willing to tear up its CDS contracts with AIG, which would have saved the taxpayers billions? Why was the information contained in the BlackRock report withheld from your November audit of the AIG counterparty payment issue?

QUESTIONS FOR MR. HABAYEB

By Ranking Member Bachus, Committee on Financial Services, participating by unanimous consent of the Committee:

1. During the fall of 2008, were you aware of the offer by Goldman Sachs to tear up its CDS contracts with AIG, which would have saved taxpayers more than $5 billion? If so, why was this option not explored or acted upon?

2. Have you been involved in any efforts to prevent disclosure of the New York Fed's assistance to AIG? Were you aware of the numerous emails from New York Fed official James Bergin that sought to gain special security status for AIG disclosures to the Securities and Exchange Commission – protections that are typically only used for national security purposes? Did you approve of these efforts? If not, who empowered Mr. Bergin with the authority to pursue obtaining possible national security status for AIG material from the SEC?

3. Were you aware of the January 13, 2009 email from Davis Polk & Wardwell attorney Diego Rotsztain that sought to ensure AIG's regulatory filings were kept secret and did "not get into the wrong hands?" Did you follow the advice of Mr. Rotsztain or approve of the efforts taken to conceal AIG's counterparty information?

4. Were you aware of the December 4, 2008 email from New York Fed official Danielle Vicente which stated that releasing AIG's counterparty information would be "politically sensitive" and that "it would be hard to sell the public on US funds to buy foreign entities out of AIG risk, especially since the foreign regulators were contacted, etc.?" This email seems to imply that foreign regulators, such as France's Commission Bancaire, were willing to negotiate on AIG's counterparty payments to such institutions as Société Générale. Were these foreign regulators, in fact, willing to negotiate? If so, please provide a complete record of all AIG communications during these negotiations.

5. Did you ever have any conversations with Secretary Geithner regarding the possible tear-up of Goldman's contracts with AIG? Was the lack of statutory authority for the New York Fed to act upon this possibility ever cited as a rationale for not accepting Goldman's willingness to tear up these contracts? If so, who was responsible for citing this lack of statutory authority?

QUESTIONS FOR MR. FRIEDMAN

By Ranking Member Bachus, Committee on Financial Services, participating by unanimous consent of the Committee:

1. During the fall of 2008, were you aware of the offer by Goldman Sachs to tear up its CDS contracts with AIG, which would have saved taxpayers more than $5 billion? If so, why was this option not explored or acted upon?

2. Have you been involved in any efforts to prevent disclosure of the New York Fed's assistance to AIG? Were you aware of the numerous emails from New York Fed official James Bergin that sought to gain special security status for AIG disclosures to the Securities and Exchange Commission – protections that are typically only used for national security purposes? Did you approve of these efforts? If not, who empowered Mr. Bergin with the authority to pursue obtaining possible national security status for AIG material from the SEC?

3. Were you aware of the January 13, 2009 email from Davis Polk & Wardwell attorney Diego Rotsztain that sought to ensure AIG's regulatory filings were kept secret and did "not get into the wrong hands?" Did you follow the advice of Mr. Rotsztain or approve of the efforts taken to conceal AIG's counterparty information?

4. Were you aware of the December 4, 2008 email from New York Fed official Danielle Vicente which stated that releasing AIG's counterparty information would be "politically sensitive" and that "it would be hard to sell the public on US funds to buy foreign entities out of AIG risk, especially since the foreign regulators were contacted, etc.?" Other than demonstrating a full understanding that the decision to withhold information was political in nature, this email seems to imply that foreign regulators, such as France's Commission Bancaire, were willing to negotiate on AIG's counterparty payments to such institutions as Société Générale. Were these foreign regulators, in fact, willing to negotiate? If so, please provide a complete record of all Federal Reserve Bank of New York communications during these negotiations.

5. Did you ever have any conversations with Secretary Geithner regarding the possible tear-up of Goldman's contracts with AIG? Was the lack of statutory authority for the New York Fed to act upon this possibility ever cited as a rationale for not accepting Goldman's willingness to tear up these contracts? If so, who was responsible for citing this lack of statutory authority?

6. During a January 26, 2009 interview with CNBC, Senator Jim Bunning claimed that the staff of the Federal Reserve was not in favor of rescuing AIG similar to the government's treatment of Lehman brothers. However, he cited an email from Chairman Bernanke to the Federal Reserve staff that served as a directive to

save AIG due to the potential risk that AIG's failure might pose to the U.S. economy. Can you confirm or deny that this differing of opinion existed between the Fed's staff and Chairman Bernanke, and do you know if this email does, in fact, exist?

QUESTIONS FOR TOM BAXTER

By Representative Marcy Kaptur:

1. In a memo obtained by the Committee from Sarah Dahlgren to you, she recommends the hiring of BlackRock Solutions to perform services for the Federal Reserve Bank of New York related to the Maiden Lane Facilities two and three. Can you tell me what Sarah Dahlgren's role was in regard to AIG?

2. Did you approve Ms. Dahlgren's request?

3. To whom at the New York Fed did BlackRock report? What level of oversight does the FRBNY have over BlackRock in its management of the three Maiden Lane facilities? Identify and provide all related documents.

4. The Committee also obtained slides where BlackRock complete an analysis of the Maiden Lane III that some counterparties were in a place to experience losses, especially if there was a downturn. Did BlackRock share this information with the Federal Reserve Bank of New York, and if so, was this information used strategically in the negotiations around the counterparty payments? Identify and provide all related documents.

5. How involved was BlackRock in the counterparty negotiations? Identify and provide all related documents.

6. Who at BlackRock did the NYFRB work with the most in regard all three Maiden Lane facilities?

7. How much profit is BlackRock expected to make managing the three Maiden Lane facilities?

8. What are you currently doing to test the firewalls put in place by BlackRock to prevent BlackRock Solutions from sharing its information with the rest of BlackRock? Did you just go on BlackRock's word or did you hire an outside entity to test the firewall – and if an entity did test this, did the firewall hold or not? Identify and provide all related documents. What do you do on a regular basis to ensure that BlackRock is not taking advantage of their management of the Maiden Lane facilities and their investment business?

9. When was the first Goldman Sachs collateral call on its CDS with AIG? What prompted this call? How soon after Goldman Sach's collateral call did other banks start making collateral calls? How many collateral calls, for what amount and from which banks rolled in on these CDS's in 2008? Why were all of the banks allowed to keep the monies received from the collateral calls on these CDS contracts in addition to the money paid to tear up the contracts?

10. What happened to the deals, including synthetic deals, that were in AIG's portfolio, getting significant collateral calls but did not go into Maiden Lane III? How much collateral has

been posted against these deals, what is their current market value and what is the plan for them in the future?

11. What is the legal analysis for why these deals were not transferred to ML III as it relates to their synthetic nature?

12. What percentage of the deals transferred to ML III consisted of underlying synthetic bonds? Is there a threshold for which the Fed had drawn that would treat some as hybrid (meaning permissible for Maiden Lane III) and some as synthetic (presumably not)?

13. What investigations is the FRBNY doing into the managers of the bad deals that ML III owns? many real investors are suing bankers and deal issuers - does the Fed or Treasury have any plans to pursue similar lawsuits against the parties responsible for such bad deals?

14. Some of the owners of the CDOs purchase by Maiden Lane III were not the banks, but their clients. The banks keep their identities closely guarded, but they are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance?

15. What analysis did they do of a rescue for the monoline insurers and why was this rejected? What communications were there with the NY insurance department and what assurances were provided as a result of these discussions? Were any strategies or data shared between the NYID and the OTS, the Fed or the Treasury? What communications and analysis were performed about the commutations executed by the monolines with counterparties such as Merrill, Calyon and Citibank?

16. What is the explanation for the appearance of the CMBS deals in Maiden Lane III? how did AIG acquire this exposure? What is Project Max, as discussed in the BlackRock memo and what were the liquidity and funding mechanisms of these bonds while in AIG's portfolio? if AIG was in a net positive funding position, why were these bonds transferred to ML III and what was the impact on AIG's balance sheet - positive or negative? what was the impact on Deutsche Bank's balance sheet? if negative for AIG and positive for DB, why were these deals included in ML III rather than kept at AIG?

17. Some of the owners of the CDOs purchased by Maiden Lane III were not the banks, but their clients. They are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance? Who were the third party clients of Goldman (and others?) who benefited from the Maiden Lane III payments to Goldman? Was any investigation performed to determine who they were and whether they were appropriate recipients of taxpayer payments? Were any conflicts of interest investigated with respect to such payments?

18. What were the hiring criteria used for selecting BlackRock as the advisor for AIG and Maiden Lane III? What was the conflicts of interest policy? How was this checked against the transactions? Identify and provide all related documents.

19. In your testimony, you discuss conversations with the credit rating agencies over AIG in particular just before the loan to AIG and following. When was the very first time that the FRBNY started a conversation with any of the rating agencies? What was the nature of the conversation? How many times did the FRBNY speak to the credit rating agencies about AIG? How many times did the FRBNY speak to the credit rating agencies about any of the counterparties of AIG? Do you have any information that any of the counterparties of AIG contacted the credit rating agencies about AIG? From your perspective, how involved were the credit rating agencies in the plan to bailout AIG, create the Maiden Lane facilities and any other related activities connected to AIG or its counterparties? Identify and provide all related documents.

QUESTIONS FOR MR. BAXTER

By Ranking Member Issa:

1. If an SEC filing by AIG on or after September 19, 2008, had violated the securities laws, should AIG have been able to avoid liability by demonstrating that all of its SEC filings were subject to review, editing, and approval by the FRBNY and its counsel? In March 2009, you suggested that AIG could avoid liability to its counterparties for revealing their identities because it was doing so at the FRBNY's direction: "If someone sues AIG, they can say the Fed told us to do it."[16] Do you believe that this immunity would extend to AIG's securities filings, which were also being directed by the FRBNY? If not, why?

2. On November 17, 2008, AIG submitted a draft SEC filing to the New York Fed and Davis Polk for review, edits, and approval. The filing reported that a new compensation package had been signed by AIG's CFO, David Herzog. Within 40 minutes, Marshall Huebner, the lead partner for Davis Polk's FRBNY business, sent an e-mail to you titled "READ ME." Huebner wrote, "Very bad timing to have this 8k come out just before the Secretary and the Chairman go before Waxman...Is there any chance—and maybe it is just too late—to get the Herzog comp package unagreed to?"[17] AIG never filed the SEC filing, and evidently canceled Mr. Herzog's compensation package. What actions did you take as a result of Huebner's e-mail?

3. Did the cancellation of Mr. Herzog's compensation package, and the cancellation of AIG's intended SEC filing, serve any aim other than avoiding embarrassment "just before the Secretary and the Chairman go before Waxman"?

4. Do you believe that it is ever appropriate for the Fed, or Treasury, to force a public corporation that has received extraordinary federal financial assistance to make changes to its compensation arrangements, or take other actions, in order to avoid making disclosures under the securities laws? When are such actions appropriate?

5. Was it appropriate for the FRBNY to contact the SEC directly to argue that a portion of AIG's filings should be kept confidential and should not even be submitted to the SEC as part of its confidentiality determination? Or should the FRBNY have allowed AIG to conduct all communication with the SEC regarding its filings on its own?

By Mr. Souder:

1. What is the purpose of an 8-K SEC filing and who bears the responsibility for AIG's financial disclosures with the SEC?

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[16] *See* FRBNY-TOWNS-R1-039070 ("If someone sues AIG, they can say the Fed told us to do it").
[17] FRBNY-TOWNS-R3-002270

2. What interest did the FRBNY have in AIG SEC's filings?

3. After September 19, 2008 AIG sent its SEC filings to the FRBNY's outside counsel, Davis Polk, for review and editing prior to submission. Is it appropriate for the FRBNY to be editing and reviewing AIG's financial disclosures?

By Ranking Member Bachus, Committee on Financial Services, participating by unanimous consent of the Committee:

1. During the fall of 2008, were you aware of the offer by Goldman Sachs to tear up its CDS contracts with AIG, which would have saved taxpayers more than $5 billion? If so, why was this option not explored or acted upon?

2. Have you been involved in any efforts to prevent disclosure of the New York Fed's assistance to AIG? Were you aware of the numerous emails from New York Fed official James Bergin that sought to gain special security status for AIG disclosures to the Securities and Exchange Commission – protections that are typically only used for national security purposes? Did you approve of these efforts? If not, who empowered Mr. Bergin with the authority to pursue obtaining possible national security status for AIG material from the SEC?

3. Were you aware of the January 13, 2009 email from Davis Polk & Wardwell attorney Diego Rotsztain that sought to ensure AIG's regulatory filings were kept secret and did "not get into the wrong hands?" Did you follow the advice of Mr. Rotsztain or approve of the efforts taken to conceal AIG's counterparty information?

4. Were you aware of the December 4, 2008 email from New York Fed official Danielle Vicente which stated that releasing AIG's counterparty information would be "politically sensitive" and that "it would be hard to sell the public on US funds to buy foreign entities out of AIG risk, especially since the foreign regulators were contacted, etc.?" Other than demonstrating a full understanding that the decision to withhold information was political in nature, this email seems to imply that foreign regulators, such as France's Commission Bancaire, were willing to negotiate on AIG's counterparty payments to such institutions as Société Générale. Were these foreign regulators, in fact, willing to negotiate? If so, please provide a complete record of all Federal Reserve Bank of New York communications during these negotiations.

5. Did you ever have any conversations with Secretary Geithner regarding the possible tear-up of Goldman's contracts with AIG? Was the lack of statutory authority for the New York Fed to act upon this possibility ever cited as a rationale for not accepting Goldman's willingness to tear up these contracts? If so, who was responsible for citing this lack of statutory authority?

6. During a January 26, 2009 interview with CNBC, Senator Jim Bunning claimed that the staff of the Federal Reserve was not in favor of rescuing AIG similar to the government's treatment of Lehman brothers. However, he cited an email from Chairman Bernanke to the Federal Reserve staff that served as a directive to save AIG due to the potential risk that AIG's failure might pose to the U.S. economy. Can you confirm or deny that this differing of opinion existed between the Fed's staff and Chairman Bernanke, and do you know if this email does, in fact, exist?

Secretary Timothy F. Geithner
Questions for the Record
House Committee on Oversight and Government Reform
January 27, 2010

Rep. Marcy Kaptur

1. **Mr. Secretary, who nominated you to be President of the Federal Reserve Bank of New York? Please describe in detail the vetting process that you experienced both before and after you were nominated.**

   The Nominating and Corporate Governance Committee of the Board of Directors nominated me to serve as President. The Committee reviews and interviews potential candidates and then makes recommendations to the full Board concerning nominations. The Committee's Charter provides detailed information about this process.[1]

2. **You stated in your testimony that after your election to be President of the Federal Reserve Bank of New York, you had to receive approval from the Chairman of the Federal Reserve Board of Governors, and that there were many checks and balances in the process. Can you please describe in full the process of approval for you – please include number of meetings, those present at each of the meetings, what was discussed, and include all related documents. I'd like to have a clear understanding the checks and balances in place and to what end these checks and balances work. Please also include a complete timeline of this approval process from start to finish.**

   As I discussed in my testimony before the Committee, the Board of Directors of the Federal Reserve Bank of New York appoints the President of the Bank, but the decision is subject to the approval of the Board of Governors of the Federal Reserve System. The members of the Board of Governors are public servants, nominated by the President and confirmed by the United States Senate. I am not aware of the details of the Board of Governors' internal deliberation process for reviewing and approving nominations.

3. **Since the inception of the Federal Reserve System in 1913, please tell me the number of Presidents of any of the twelve Federal Reserve Banks that were elected by the Board of on of the 12 the Reserve Banks and subsequently did not receive the approval of the Chairman of the Federal Reserve Board of Governors.**

   I have no personal knowledge about this historical data.

4. **This question concerns the Federal Reserve and Treasury decisions on the creation of a special purpose vehicle called Madden Lane III that bought the underlying collateral of a portion of AIG's credit default swaps for the claimed purpose of preventing further collateral calls, an easing on AIG's liquidity pressures and a strengthening of the financial system.**

   The Special Inspector General for the Troubled Asset Relief Program reported on November 17, 2009 (SIGTARP-10-003) there were payments to AIG Credit Default Swap Counterparties of $27.1 billion (Table 2, page 20).

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[1] Nominating and Corporate Governance Committee Charter, Federal Reserve Bank of New York, *available at* http://www.newyorkfed.org/aboutthefed/nominate.html.

Of the 16 banks that were recipients of the payments, 12 were foreign. Of the $27.1 billion in payments, the foreign-based banks received $16.6 billion or 61.2 percent of the funds. Goldman Sachs received $5.6 billion (18.8) percent and the balance (20 percent) went to Merrill Lynch, Wachovia and Bank of America

A. **Did U.S. taxpayers and their government have any legal or contractual obligation to make payments to these AIG Credit Default Swap Counterparties?**

In late 2008, AIG faced the prospect of default and bankruptcy, which would have had catastrophic consequences for the economy. AIG was the largest provider of conventional insurance in the world, with approximately 75 million individual and corporate customers in over 130 countries. If AIG had failed, the crisis would have almost certainly spread to the entire insurance industry. The government took action to prevent AIG's failure and to protect the financial system. This included helping restructure the credit default swap contracts that AIG had entered into with various counterparties.

As I described in my testimony before the Committee, AIG's parent holding company, which was largely unregulated, had engaged in a broad range of financial activities that strayed well beyond the business of life insurance and property and casualty insurance. AIG's Financial Products subsidiary (AIGFP) expanded into some of the newest, riskiest, and most complex parts of the financial system.

AIG had agreed to insure the value of certain risky securities called multi-sector collateralized debt obligations (CDOs). The value of these securities was tied to other assets, mostly subprime mortgages. As the financial crisis intensified in 2008, the value of the securities fell sharply and AIG incurred losses on these contracts and had to post collateral or make payments on the insurance. AIG had a legal obligation to make these payments, and the failure to fulfill its obligation to any counterparty – domestic or foreign – would have resulted in its default and collapse.

To help prevent this, the Federal Reserve Bank of New York (FRBNY) helped establish and fund Maiden Lane III. The purpose of this new company was to purchase troubled assets that AIG had either acquired or insured, and to manage those assets for the benefit of the taxpayer. Purchasing those assets removed significant exposure from AIG's balance sheet and helped prevent the company from being downgraded and failing. In designing and implementing this transaction the main objective of the Federal Reserve was, as it always is, to achieve the best possible result for the taxpayer.

Since the Maiden Lane companies purchased these securities, they have generated significant cash flows that have been used to pay down the FRBNY's loan by more than 25 percent. We expect Maiden Lane III to pay the FRBNY back in full. I believe that the strategy that the Federal Reserve and the Treasury pursued in establishing Maiden Lane III will generate a better outcome than the other alternatives available to us at that time.

B. Did the Federal Reserve or Treasury contact the home governments or central banks of the foreign banks and request their assistance in providing these payments?

I am not aware of any such contacts.

C. If demands on these foreign authorities were made, what were their responses?

Please see the answer to Question 4.B above.

D. If demands on foreign authorities were not make, why not?

As described in the answer to Question 4.A above, the actual payments to the counterparties were made by Maiden Lane III, funded by AIG and a loan from the Federal Reserve Bank of New York. They were commercial transactions, required under the contractual obligations that AIG had created when it insured the securities.

Seeking the assistance of foreign governments to help with the restructuring of AIG's balance sheet and the purchase of the troubled assets would have been time consuming, with little likelihood of success. AIG's financial position was deteriorating rapidly, and the prospect of a further ratings downgrade was imminent. AIG was scheduled to report a $25 billion loss for the third quarter on November 10, and the ratings agencies had informed AIG that, absent a parallel announcement of solutions to its liquidity and capital problems, they would downgrade the company yet again. Such a downgrade would have led to AIG's failure and could have triggered the catastrophic damage to the U.S. financial system that the government had been working to prevent since September 2008.

E. Was Congress informed of the decision to make these payments beforehand and if so to whom, how and when?

In accordance with the authority provided in section 13(3) of the Federal Reserve Act, the Federal Reserve Bank of New York made the decision after consultation with and approval of the Federal Reserve Board of Governors. The Federal Reserve announced the decision publicly on November 10, 2008, and the securities were purchased on November 25 and December 18, 2008. I am unaware of whether anyone in the Federal

Reserve System notified Congress of the decision prior to November 10, 2008.

5. **Did anyone advise you that you should recuse yourself when President-elect Obama informed you of his intention to nominate you to be Treasury Secretary? If "yes", provide their names and the date, content and context of their advice and any related documents.**

On November 24, 2008, President-elect Barack Obama announced that he intended to nominate me to be Secretary of the Treasury. I discussed the situation with the Chairman of the Federal Reserve Board, the General Counsel of the Federal Reserve Board, the General Counsel of the FRBNY, and the Chairman of the Board of Directors of the FRBNY, among others. I was asked to stay on as President of the FRBNY on an interim basis, which I did. I am not aware of any legal reason that would have made it necessary for me to stop conducting my duties as President. The decision to withdraw from certain activities was made, out of an abundance of caution, in part to protect the independence of the FRBNY, and, in part, because of the time demands that I was going to face in helping to shape the President-elect's economic strategy. Specifically, starting on November 24, 2008, I withdrew from involvement in monetary policy decisions, policies involving individual institutions, and day-to-day management activities.

6. **Did you seek or receive legal advice or the expert ethical advice as to whether and how you should recuse yourself? If "yes", provide their names and date, content, and context of their advice and any related documents. If "no", why did you not seek such advice?**

Please see the answer to Question 5 above.

7. **When and how did you advise the Office of Government Ethics (OGE) of your recusal? Provide any related documents.**

I was not required to advise the Office of Government Ethics of my recusal, and I did not do so.

8. **Explain in detail why you recused yourself and the exact nature and language of the activities which you recused yourself from performing. Explain why those activities posed a potential ethical problem absent recusal. Provide all related documents.**

Please see the answer to Question 5 above.

9. **Who did you appoint in your recusal to perform the duties from which you were recusing yourself? How did you inform them, and the Federal Reserve Bank of New York and the Board of Governors of the Federal Reserve, of your recusal and the appointment of your substitute decision makers? Provide all related documents.**

In accordance with established practice, my colleagues and staff, led by First Vice President Christine Cumming, carried out the day-to-day management operations of the Federal Reserve Bank of New York. Ms. Cumming is the second ranking officer in the Bank, and also serves as its chief operating officer. Management and staff at the Bank also worked in close cooperation with their colleagues at the Federal Reserve Board.

10. When and how did you inform the incoming incoming Obama administration of your recusal? What was their response? Provide all related documents.

I discussed my decision to withdraw from monetary policy decisions, policies involving individual institutions, and day-to-day management activities with advisers of the President-elect. As I described above in the answer to Question 5, this decision was made, in part, to protect the independence of the Federal Reserve, in part, because I was going to be dedicating the bulk of my time to helping shape the President-elect's economic strategy.

11. Why did you fail to recuse yourself in writing? When and how did you become aware of the requirement to confirm any recusal in writing? Provide all related documents.

As discussed above in the answer to Question 5, I withdrew from involvement in monetary policy decisions, policies involving individual institutions, and day-to-day management activities. My colleagues and staff were aware of this decision. I am not aware of any requirement to confirm such a recusal in writing.

12. Who did your recusal identify as the official(s) to screen communications in order to make the recusal effective (as required under OGE rules)? OGE takes the position that recusal requires the official to appoint screeners to prevent the recused official of being involved even in communications, not simply decisions, concerning the subjects of the recusal. Did you recuse yourself from any involvement, including the receipt of information, related to the subjects from which you recused yourself? If not, why not? Provide all related documents.

As discussed in the answer to Question 5 above, I am not aware of any reason that would have made it legally necessary for me to stop conducting my duties as President, but out of an abundance of caution, I withdrew from certain activities. My colleagues and staff were aware of this decision.

13. When did you first make public your recusal? Did you direct, urge, or imply that your recusal not be made public? Provide full details and all related documents.

There was no formal public announcement of the decision, but it was widely known. For example, on December 1, the Federal Reserve Bank of New York issued a press release stating that it would begin a search for a new President in light of my nomination. The announcement also noted that First Vice President Christine Cumming had taken over my responsibilities regarding monetary policy decisions.[2] Contemporaneous news accounts also reported on these events.

14. Do you concede that your recusal procedures failed to comply with the law and best ethical practices?

No. I believe that my decision to withdraw from monetary policy decisions, policies involving individual institutions, and day-to-day management activities was consistent with the law and the best ethical practices.

15. Explain fully and in detail the potential conflicts of interest that could have arisen from your participation in decisions concerning AIG. Provide any related documents.

As discussed in the answer to Question 5 above, I am not aware of any legal reason that would have made it necessary for me to stop conducting my duties as President, but out of an abundance of caution, I withdrew from certain activities. The decision did not relate to potential conflicts about any particular matter. This decision was made in part to protect the independence of the FRBNY, and, in part, because of the time demands that I was going to face in helping shape the President-elect's economic strategy.

16. By recusing yourself from regulatory activities in November 2008, during what you describe as a crisis that threatened a second Great Depression, you removed the most senior field regulator of many of the largest bank holding companies at a time when your expertise was most critical. Provide a list of the bank holding companies and state chartered member banks with assets over $1 billion that the Federal Reserve Bank of New York (FRBNY) regulated at the time of your recusal. Why did you believe that the potential conflicts of interest were so severe that they compelled you to recuse yourself during this desperate crisis? Provide any written or electronic explanation of your decision prior to your testimony.

The leadership team at the Federal Reserve Bank of New York is deeply experienced. As I discussed above in the answer to Question 9, when I withdrew from certain activities, First Vice President Christine Cumming led the day-to-day operations of the Federal Reserve Bank of New York.

Ms. Cumming is the second ranking officer in the Bank and has over thirty years experience working there. Under the circumstances, I believe that my decision to withdraw from certain management and policy activities at the Bank was in the best interest of both the Federal Reserve Bank of New York and the American people.

17. Provide in detail, with any related documents, your understanding of the business strategy of each AIG CDS counterparty in its dealings with AIG, the Fed, or any U.S.

[2] Federal Reserve Bank of New York, Press Release, *New York Fed Initiates Search for New President*, December 1, 2008, *available at* http://www.ny.frb.org/newsevents/news/aboutthefed/2008/oa081201.html.

agency with regard to obtaining full payment on its CDS. Identify and provide all related documents.

Due to the nature of the contracts that AIG had entered into when selling insurance on the troubled securities, the contractual rights of the counterparties were very well protected. The counterparties had purchased insurance from AIG that entitled them, as a matter of law, to the full or par value of the contracts.

In addition, the contracts between AIG and the counterparties afforded the counterparties the right to payments of cash collateral under certain circumstances. As a consequence, the value of the securities that the counterparties held, combined with the collateral that they had already obtained from AIG was generally equal to the par value of the securities. If AIG had defaulted, or even filed for bankruptcy, the counterparties would have kept both the collateral and the underlying securities.

18. If the counterparties had forced AIG into bankruptcy, what was AIG's, Treasury's, the Fed's, and the FRBNY's analyses of how large their recovery would have been on the CDS. Provide all such analyses and identify the dates on which they were conducted and who received such analyses. What analyses did you order of how much each counterparty would receive should AIG declare bankruptcy? When did you request or direct such analyses to be conducted? Who prepared them and when did they report their results? What were those results? Identify and provide all related documents.

As I discussed in the answer to Question 17, the contractual rights of the counterparties were very well protected. The counterparties had purchased insurance from AIG that entitled them, as a matter of law, to the full or par value of the contracts.

In addition, the contracts between AIG and the counterparties afforded the counterparties the right to payments of cash collateral under certain circumstances. As a consequence, the value of the securities that the counterparties held, combined with the collateral that they had already obtained from AIG was generally equal to the par value of the securities. As a result, if AIG had defaulted on its contractual obligations, or even filed for bankruptcy, the counterparties would have kept both the collateral and the underlying securities.

For additional information about the analysis, I would refer you to the testimony before the Committee by Thomas Baxter, General Counsel and Executive Vice President of the Federal Reserve Bank of New York.[3]

19. Do you agree that if the counterparties had forced AIG into bankruptcy they were likely to suffer large losses on their CDS? If not, provide a detailed explanation of your rationale. Identify and provide all related documents.

As discussed in the answer to Question 18 above, if AIG had defaulted, or even filed for bankruptcy, the counterparties would have kept both the cash collateral payments that they

[3] Thomas C. Baxter Jr., *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Testimony before the Committee on Government Oversight and Reform, January 27, 2010.

had previously received from AIG as well as the underlying securities (the CDOs). If the value of the underlying securities had continued to fall, the counterparties would have had a claim against AIG under the credit default swaps to make up the difference. On the other hand, if the price of the securities improved – as our analysis indicated was likely over the medium to long run – the counterparties would have received more than par in the transaction. Instead, with our assistance, the insurance contracts were terminated, and the counterparties transferred the securities to Maiden Lane III, which has managed the securities to the benefit of U.S. taxpayers.

20. Do you agree that the U.S. government had unprecedented leverage with regard to the AIG CDS counterparties given the government bailout of AIG and many of the AIG counterparties? If not, provide a detailed explanation of your rationale?

No. In fact, we had very little negotiating leverage. For the reasons discussed in the answers to Questions 18 and 19 above, the counterparties were in a very strong position and generally protected in the event of AIG's default. They held insurance contracts entitling them to full or par value of the contracts. If AIG had defaulted, or even filed for bankruptcy, the counterparties would have kept both the cash collateral payments that they had previously received from AIG as well as the underlying securities.

Further, we were in the midst of a severe economic crisis. In a normal environment, regulators may have had more time to try to help solve the problem in other ways. In the environment that existed, we had to act quickly and resolve a threat to AIG's liquidity and balance sheet that would likely have otherwise resulted in an immediate downgrade and failure.

As I discussed in my testimony, some have suggested that the FRBNY should have used its regulatory authority, or some other means, to effectively coerce AIG's counterparties to accept concessions. This was not a viable option either. Once a company refuses to meet its full obligations to a customer, other customers will quickly find other places to do business. If we had sought to force counterparties to accept less than they were legally entitled to, market participants would have lost additional confidence in AIG and the ratings agencies would likely have downgraded AIG again. This could have led to the company's collapse, threatened our efforts to rebuild confidence in the financial system, and meant a deeper recession, more financial turmoil, and a much higher cost for American taxpayers. The Federal Reserve had already acted to rescue AIG from insolvency, and the counterparties fully expected that we would stand by that decision.

We knew that the likelihood of success in the negotiations was modest. Relatively quickly, and not unexpectedly, we discovered that most firms would not provide a concession under any circumstances. One counterparty said that it was willing to provide a very minor concession, but only if every other counterparty would also agree to equal concessions on their prices.

In the end, the prices paid for the securities were their fair market value, and because the counterparties retained the collateral they had previously received from AIG, they all received an aggregate amount equal to par value of their securities. In return, the insurance contracts were terminated, and the counterparties transferred the securities to Maiden Lane III. In designing and implementing the transaction to restructure the contracts, our main objective was, as it always is, to get the best deal for the taxpayer. We made judgments about these transactions carefully with the advice of outside counsel and financial experts.

Documents related to these questions and related topics would be in the possession of the Federal Reserve Bank of New York.

21. **Describe in detail your analysis of how the U.S. government could have best used its leverage to avoid paying roughly 100 cents on the dollar for the CDS had that been your mission. Identify and provide all related documents.**

    Please see the answer to Question 20 above.

22. **Why didn't the U.S. use its roughly 80 percent ownership of AIG to spin off AIG's trading arm and place it in bankruptcy? Describe in detail the U.S. government (including the FRBNY and the Fed) and AIG research into its bankruptcy options for AIG. Identify and provide any advice, including legal advice, that the U.S. government or AIG received concerning such a potential spin off and bankruptcy filing by the trading arm.**

    As I discussed in my testimony, there was no legal tool available to handle the failure of a company like AIG, comparable to the one available to the Federal Deposit Insurance Corporation for managing the orderly wind-down of a troubled bank. In addition, we did not have the ability to separate the stable underlying insurance businesses from the complex and highly risky financial activities carried out primarily by the parent holding company. Experts suggested that achieving that separation would take several years.

    The financial reform proposals put forth by President Obama and reflected in H.R. 4173 address these regulatory shortcomings. I commend the Members of this Committee for advancing financial reform to this point, and I look forward to continuing to work with you to enact a strong set of comprehensive reforms.

23. **Did the U.S. government (including the Fed and the FRBNY) take any action to demand that the AIG CDS counterparties cease demands that AIG post additional collateral? If not, why not? If they did, describe the efforts (and the response of the counterparties) fully. Identify and provide all related documents.**

    The counterparty negotiations were conducted in connection with the formation and funding of Maiden Lane III. AIG had entered into insurance contracts with various third parties to protect the value of certain risky securities, called multi-sector collaterized debt obligations (CDOs), in exchange for periodic premium payments. The value of these securities was tied to pools of other assets, mostly subprime mortgages. The contracts required AIG to provide its counterparties collateral as the market value of the underlying CDOs, the credit rating of the assets behind the CDO, or AIG's credit rating declined. As the financial crisis intensified, each of these events occurred. As of November 5, 2008, AIG had already posted approximately $37 billion in collateral against these exposures in accordance with the terms of the contracts, and these collateral calls contributed significantly to the $25 billion in losses that AIG reported for the third quarter of 2008. By purchasing the underlying securities, Maiden Lane III removed the persistent threat that these contracts posed to AIG's continuing viability.

Coercing AIG's counterparties to accept concessions on the value of the securities was not a viable option for several reasons. First, if the FRBNY had tried to force counterparties to accept less than they were legally entitled to, market participants would have lost additional confidence in AIG leading to the company's failure. Once a company refuses to meet its full obligations to a customer, other customers will find other places to do business.

Second, the counterparties were in a strong bargaining position. They could have refused to grant such concessions, kept the collateral they had already received, kept the CDO securities that AIG had insured, and sued AIG for breach of contract. This would have increased the taxpayer's potential exposure and precluded them from benefiting from any recovery in the value of the CDOs, which has in fact happened.

Third, if the FRBNY had attempted to use its regulatory authority to coerce or extract concessions from AIG's counterparties, that attempt would likely have led to a further downgrade of AIG's ratings, precisely the result that all of the government's actions were intended to avoid. An "investment grade" credit rating is the rating agencies' judgment that creditors will likely be repaid in accordance with the terms of their contracts, not according to a hypothetical government-coerced discount. If the FRBNY had attempted to force counterparties to accept less than they were legally entitled to, then AIG would likely have lost its "investment grade" rating. Such a downgrade could have led to the obligation for more collateral payments, and would have likely led to the company's collapse. This would have threatened government efforts to rebuild confidence in the overall financial system, and meant a deeper recession, more financial turmoil, and, ultimately, a much higher cost for American taxpayers.

24. What monitoring of AIG's exposure to CDS written on CDOs did NY Fed undertake in

a. 2004-2006
b. H1 2007 after HSBC mortgage blowup
c. H2 2007 after Bear Stearns Hedge Fund blowup
d. Q1 2008 after monoline distress
e. Q2 2008 after Bear blowup and acute monoline distress
f. Q3 2008 in run up to collateral calls on AIG?

subject to result of above questions). The following blog entry, by an anonymous securities lawyer familiar with the terrain, criticizes a financial journalist for obliviousness to the level of risk at AIG in mid-2007, pointing to a widely distributed Fitch report that highlight's AIG's exposure. AIG was well known as a major, if not the major, credit default swaps counterparty. Certainly by the time of the Bear Stearns rescue, if not sooner, credit default swaps were recognized as a source of

systemic risk; if nothing else, Eric Dinallo of New York State Deptment of Insurance made that clear in January 2008. Why was there no interest in AIG as a source of counterparty risk to the dealer community?
http://economicsofcontempt.blogspot.com/2009/09/risk-held-at-aigfp-was-not-surprise.html

The Federal Reserve did not and does not have supervisory authority over AIG or any of its subsidiaries. The Federal Reserve was first notified of the extent of the impending liquidity crisis at AIG on Friday, September 12, 2008, by officials of AIG. On that date, AIG officials met with senior officials at the Federal Reserve Bank of New York and the Board to discuss the company's liquidity position. Before then, the Federal Reserve was aware of general concerns regarding the financial health of AIG through ongoing interaction with market participants and banking organizations that it supervised, as well as press reports and other public materials. However, prior to this date, the Federal Reserve did not have access to the type of proprietary, confidential company information needed to understand the true severity and immediacy of AIG's liquidity needs, nor had any person (including AIG) requested that the Federal Reserve provide emergency credit to AIG under section 13(3) of the Federal Reserve Act.

25. On what date did Treasury start making contingency plans for a run on AIG? What the NYFRB involved?

AIG informed the Federal Reserve and the Department of the Treasury about the extent of its impending liquidity crisis on September 12, 2008. We immediately brought together a team of people from the Federal Reserve, the Treasury, and the New York State Insurance Department to work together to evaluate how to respond to AIG's problems and prevent its collapse.

Under the system of financial regulation in place in 2008, the Federal Reserve had no role in supervising or regulating AIG. But Congress had given the Federal Reserve authority to provide liquidity to the financial system in times of severe stress. The Federal Reserve acted to fulfill that responsibility with respect to AIG after it learned that the company was facing potentially fatal liquidity problems.

26. On what date did Treasury begin liaison with AIGFP's regulator UK's FSA? What the NYFRB involved?

Although it had an office located in London, I do not believe that AIG's Financial Products subsidiary (AIGFP) was regulated by the Financial Service Authority (FSA).

27. On what date did Treasury start the process of discovering who AIG's counterparties were for the CDS's written on CDO's by AIG? What the NYFRB involved?

On Friday, September 12, 2008, AIG officials informed the Federal Reserve and the Treasury that the company was facing potentially fatal liquidity problems. As described in the answer to Question 25 above, we immediately brought together a team of people from the Federal

Reserve, the Department of the Treasury, and the New York State Insurance Department to evaluate AIG's systemic importance. As part of this process, the team reviewed information about AIG's exposure through its insurance contracts and credit default swaps. At the time, these totaled over $2 trillion of notional derivative exposures, through thousands of individual insurance contracts.

28. What risk modeling or other assessments did Treasury undertake of the resulting systemic risk and when did they start? What the NYFRB involved?

As discussed above in the responses to Questions 24 and 25, AIG officials informed the Federal Reserve and the Treasury on Friday, September 12, 2008, that the company was facing potentially fatal liquidity problems. We immediately brought together a team of people from the Federal Reserve, the Department of the Treasury, and the New York State Insurance Department to evaluate AIG's systemic importance.

The team addressed the fundamental question of how the failure of AIG would affect the financial system and the broader economy. The failure of AIG in the fall of 2008 would have imposed significant financial losses on many individuals, households, and businesses; shattered confidence in already fragile financial markets; and greatly increased fear and uncertainty about the viability of our financial institutions.

29. What legal advice did Treasury take regarding the prospect of successfully challenging the French claim that settling the AIG CDS on CDOs for 100 cents on the dollar would be illegal under French law?

In November 2008, the Federal Reserve extended credit to Maiden Lane III to address the increasing liquidity strains faced by AIG resulting from its obligation to post collateral with the counterparties to credit default swaps and other derivatives contracts written by AIG's Financial Products subsidiary. In connection with this restructuring, the Federal Reserve undertook to obtain concessions from the counterparties, but was unable to obtain such agreements.

As I described in my testimony before the Committee, and as Chairman Bernanke described in his letter to Senators Dodd and Shelby dated January 19, 2010,[4] as part of this effort, Federal Reserve Bank of New York officials contacted the Commission Bancaire, the French bank regulator, to inform it that the Federal Reserve Bank of New York was conducting negotiations with two French banks, Societe Generale and Calyon. The Commission Bancaire is an arm of the French government that is charged with supervising French banks and administering and enforcing French banking laws. It has the power to impose administrative penalties and financial sanctions on offenders.

The Commission Bancaire informed FRBNY officials that under French law, unless AIG went into bankruptcy, the French banks could not voluntarily agree to accept less than par

[4] Letter from Ben S. Bernanke, Chairman of the Board of Governors of the Federal Reserve System to the Honorable Christopher J. Dodd and the Honorable Richard C. Shelby, January 19, 2010.

value for the underlying securities in exchange for terminating the contracts. The French banks informed FRBNY officials of this as well.

30. Is it correct that you claimed at the time that legal obstacles faced by the French banks were a major reason why haircuts could not be negotiated?

No, we did not rely on that argument. There were many different factors that affected the outcome. Most of the firms would not, on any condition, agree to provide concessions. For additional information, please refer to the answer to Question 20 above.

31. Are you aware that it has since become clear that those legal difficulties were fictitious?

The French Commission Bancaire told Federal Reserve Bank of New York officials unequivocally that, under French law, absent an AIG bankruptcy, the banks were prohibited from voluntarily agreeing to accept less than par value for the underlying securities in exchange for terminating the swap contracts. I am not aware of any evidence that the Commission's legal position was fictitious or untrue.

32. Considering how Socgen and Calyon were both very closely linked to US banks in particular, over half of SocGen's exposure was underwritten by Goldman, for example], is it possible that US banks knew about or encouraged French banks to urge their regulators to represent their legal situation falsely? Do you think an investigation might be warranted?

I am not aware of any such conduct. As discussed above in the answer to Question 18, the contractual rights of all of the AIG counterparties were clear. The contracts afforded the counterparties the right to cash payments of collateral from AIG. And if AIG had defaulted on the contracts, the counterparties would have been entitled to keep both the collateral payments and the underlying securities.

33. Some of the owners of the CDOs purchase by Maiden Lane III were not the banks, but their clients. They are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance? Who were the third party clients of Goldman (and others?) who benefited from the Maiden Lane III payments to Goldman? Was any investigation performed to determine who they were and whether they were appropriate recipients of taxpayer payments? Were any conflicts of interest investigated with respect to such payments?

Maiden Lane III was established to purchase troubled assets that AIG had either acquired or insured, and to manage those assets for the benefit of the taxpayer. The counterparties held insurance that entitled them to full or par value of the contracts. Purchasing the assets removed significant exposure from AIG's balance sheet and helped prevent the company from failing. The purpose of restructuring the contracts was to prevent AIG from defaulting and going into bankruptcy, not to benefit any individual counterparties, banks, or their clients. All counterparties were treated equally. Attempting to selectively default on any contract would have resulted in a downgrade, general default, and the failure of AIG.

34. Why did you as President of the Federal Reserve Bank of New York not work out an arrangement to remove the AIGFP until from the company and dealing with it separately rather than allow the AIGFP unit to infect the entire company?

As discussed above in the answer to Question 22, there was no regulatory tool available to the Federal Reserve at the time to handle the failure of AIG that was comparable to the one available to the Federal Deposit Insurance Corporation for managing the orderly wind-down of a troubled bank.

Legally, AIG was liable for all of the contracts into which its AIGFP subsidiary had entered. The obligations were interwoven within the corporate structure. We did not have the ability to separate the underlying insurance businesses from the complex and dangerous financial activities carried out primarily by the parent holding company. AIG's insurance subsidiaries were interconnected with the parent company and its unregulated affiliates both financially and operationally. Experts suggested that achieving a separation would take several years.

35. The AIG transaction was disturbing to many observers. Why did out government not require the bank creditors to take the lead and bear the loss in our plan to stabilize AIG? You in effect nationalized the company and let the creditors off the hook?

The Federal Reserve and the Treasury determined that it was in the best interests of the United States to rescue AIG in order to stop the panic and prevent further damage to the economy. Without assistance, AIG would have been forced to file for bankruptcy protection, resulting in default of over $100 billion of debt, as well as trillions of dollars of derivative contracts. The failure of AIG would have been catastrophic for a financial system already in free fall.

36. What's the propriety of the taxpayers, via our subsidy to AIG, paying UBS $5 billion while the Justice Department was prosecuting it for massive tax fraud?

Counterparties, such as UBS, held insurance that entitled them to full or par value of the contracts. AIG's contractual obligation to fulfill the contracts was not affected by actions or investigations by the Department of Justice with regard to a particular counterparty. The contracts were commercial transactions between private entities.

Moreover, the purpose of paying the counterparties to terminate the credit default swap contracts and turn over the underlying securities was to remove a substantial threat to AIG's liquidity and solvency, while allowing taxpayers to benefit from any recovery in the securities. Taxpayers benefitted in at least two respects from these transactions: (i) AIG was stabilized, thereby removing a significant threat to our financial system and economy; and (ii) the price of the transferred securities has improved, which translates into repayments and potential profits from loans to Maiden Lane III.

37. In the hearing did you say that losses to the banks would not have been material had AIG not paid 100 cents on the dollar – that makes paying 100 cents on the dollar insane? Any reasonable party could have negotiated a better deal. Other financial troubled entities paid 13 cents on the dollar for their CDS's.

We had very little negotiating leverage. For the reasons discussed in the answers to Question 20 and others above, the counterparties were in a very strong position. They held insurance contracts entitling them to full or par value of the contracts. And they were generally protected on the value of the contracts even in the event of AIG's default. If AIG had defaulted, or even filed for bankruptcy, the counterparties would have kept both the cash collateral payments that they had previously received from AIG as well as the underlying securities.

But losses to the specific firms were not the issue. At the time, the government was working to save AIG and rebuild confidence in the financial system. The FRBNY could not credibly threaten not to pay the counterparties without being willing to follow through on that threat and put AIG into bankruptcy. At the time, any suggestion that it might let AIG fail would have worked against the vital aim of restoring stability and confidence in the financial system.

Moreover, we had very little time to act. AIG's financial position was deteriorating rapidly, and the prospect of a further ratings downgrade was imminent. AIG was scheduled to report a $25 billion loss for the third quarter on November 10, and the ratings agencies had informed AIG that, absent a parallel announcement of solutions to its liquidity and capital problems, they would downgrade the company's credit rating. Such a downgrade would have led to AIG's failure and triggered the catastrophic consequences the government had been trying to avoid since September 2008.

A bankruptcy would have entitled the counterparties to terminate the credit default swap contracts and keep the collateral that AIG had previously posted, as well as the underlying collateralized debt obligations that AIG had insured. By contrast, the prices paid for the securities were their fair market value. In return, the insurance contracts were terminated, and the counterparties transferred the securities to Maiden Lane III.

38. Mr. Secretary, in your previous position, what did you do during the negotiations with AIG's counterparties to get the counterparties to accept less than 100 cents on the dollar, if anything? Were you working to make whole the Wall Street member banks, the Federal Reserve System, the American people, or none of the above?

For more information about the constraints that we faced in the negotiations with the counterparties, please see the answers to Questions 23 and 37 above.

In response to the second part of the question, the steps the government took to rescue AIG were motivated solely by what we believed to be in the best interest of the American people. We did not act because AIG asked for assistance. We did not act to protect the financial interests of individual institutions. We acted because the consequences of AIG failing at that time, in those circumstances, would have been catastrophic for our economy and for American families and businesses. In designing and implementing the transactions, the main objective was to get the best deal for the U.S. taxpayer.

39. The CEO of Goldman Sachs was asked at the Financial Crisis Inquiry Commission if the government had asked Goldman to participate in the rescue of AIG. He responded "Not to my knowledge." In hindsight, what would you change at of the AIG transactions? Was there a better way to calm the markets without doing so much damage to the company and destroying so much value?

The Maiden Lane transactions did not destroy value, they preserved value. Under very difficult circumstances, amidst a crisis of confidence in the financial system, we pursued the best practical course that we had available.

40. Why did the U.S. government limit its role to facilitate a sector solution rather than destroying the entire company by nationalizing it?

The goal of the government intervention was to prevent the company's collapse and maintain the continuous operations of its insurance businesses. AIG was the largest provider of conventional insurance in the world. The rescue plan succeeded in keeping them operational and averting the catastrophic consequences that would have resulted from AIG's default and failure. There was no capacity for a consortium of private firms to find the resources necessary to solve the crisis without government assistance because of both the scale of AIG's losses and financial needs, and because of the force of the storm enveloping the rest of the financial system.

We did not nationalize the company. We provided necessary assistance during the crisis in order to keep its basic insurance business in operation, and we succeeded. Today, AIG's insurance operations are generating positive returns. In addition, AIG recently reached agreements to sell two of its largest foreign life insurance subsidiaries (AIA and Alico). AIG plans to use the proceeds from those sales and profits from its restructured operations to repay some of the support that the government has provided.

41. Mr. Geithner, according your phone log, Congressman Rahm Emanuel 3:30 pm Sept. 16. What events were transpiring related to crisis at that point? What had happened previously? What was the nature of that call?

During the time that I served as President of the Federal Reserve Bank of New York, I communicated with many different members of Congress to keep them apprised of events and developments in the financial markets. As you can see from my telephone logs, I participated in hundreds of phone calls during the financial crisis. At the time, Congressman Emanuel was serving as Democratic Caucus Chairman, an important leadership role in the Congress, and we conferred about the financial crisis on a number of different occasions. To the best of my recollection, the conversations with then-Representative Emanuel you reference were to discuss developments during the crisis and the steps the government was taking to address those developments.

42. **You next spoke to Congressman Emanuel at 10:05 on Sept. 22 sandwiched in between Mr. Mack at 7:27, Mr. Blankfein at 7:56, Chairman Bernanke at 8:00, Secretary Paulson at 8:19, Mr. Pandit at 8:25, Mr. Dimon at 8:32, Secretary Paulson at 9:39, Hector Sants at 9:47, Rahm Emanuel at 10:05, Bob Rubin at 10:10, Alan Greenspan at 11:09, and Rubin again at 12.57. That seems like an important day. Why Emanuel and not Pelosi?**

    Please see the answer to Question 41 above.

43. **Next is Sept. 24, sandwiched in between Mr. Rubin at 8:12, Mr. Summers at 8:35, Congressman Emanuel at 10:26, Mr. Altman at 10:56, Secretary Paulson at12:22, and again Mr. Rubin at 12:47. What was the nature of these calls and why Congressman Emanuel and not other Members in Congressional Leadership positions?**

    Please see the answer to Question 41 above.

44. **Why did you not get involved in the negotiations to seek concessions from the counterparties?**

    FRBNY staff and the experts that the Federal Reserve retained are talented and experienced negotiators. However, they faced many serious constraints in dealing with the counterparties. These are discussed in the answers to Questions 23 and 37 above.

Rep. Darrell Issa

1. **Were you aware that the FRBNY, starting on September 19, 2008, required AIG to submit all "SEC filings, press releases, and other significant communications" to its counsel, Davis Polk & Wardwell ("Davis Polk"), for edits and approval?[5] If you were aware of this policy, did you approve it? If you were unaware of this policy at the time, do you now believe that it was appropriate? If you had known that your staff would insist on restricting AIG's disclosures, would you have made sure that AIG was given more autonomy?**

   I was not involved in any decisions regarding AIG's securities filings. But I know that the Federal Reserve Bank of New York staff who were involved are people of enormous integrity and experience. I trust that they acted appropriately under the circumstances.

   For answers to these questions, I would refer you generally to the testimony before the Committee by Thomas Baxter, General Counsel of the Federal Reserve Bank of New York,[6] as well as the *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, dated January 19, 2010.[7]

2. **If an SEC filing by AIG on or after September 19, 2008, had violated the securities laws, should AIG have been able to avoid liability by demonstrating that all of its SEC filings were subject to review, editing, and approval by the FRBNY and its counsel? Would you have agreed or disagreed with your FRBNY General Counsel, Thomas Baxter, when he suggested that AIG could avoid liability for statements made at the direction of the FRBNY?[8]**

   You are asking a hypothetical legal question, and I do not have the expertise to make a legal conclusion about it. I was not involved in any decisions about AIG's securities filings. As discussed in the answer to Question 1, I would refer you to the testimony before the Committee by Mr. Baxter,[9] as well as the *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, dated January 19, 2010.[10]

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[5] *See* FRBNY-TOWNS-R3-002263-64.
[6] Thomas C. Baxter Jr., *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Testimony before the Committee on Government Oversight and Reform, January 27, 2010.
[7] Federal Reserve Bank of New York, *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, January 19, 2010, *available* at http://www.newyorkfed.org/markets/st100119.html.
[8] *See* FRBNY-TOWNS-R1-039070 ("If someone sues AIG, they can say the Fed told us to do it").
[9] Thomas C. Baxter Jr., *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Testimony before the Committee on Government Oversight and Reform, January 27, 2010.
[10] Federal Reserve Bank of New York, *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, January 19, 2010, *available* at http://www.newyorkfed.org/markets/st100119.html.

3. **Were you aware that the FRBNY, as of November 11, 2008, did not want to disclose that AIG's CDS counterparties were going to receive the par value of the underlying assets in the Maiden Lane III transactions? [11] Did you order your staff not to disclose this fact? If you were unaware that the FRBNY did not want to disclose this fact, do you now believe this non-disclosure was appropriate?**

   I had no role in making decisions regarding what to disclose about the specific financial terms of Maiden Lane III or the payments to AIG's counterparties. But I believe that the people involved are people of enormous integrity and experience.

4. **Were you aware that the FRBNY specifically ordered AIG not to disclose, in its SEC filings, that its counterparties received par value? [12] Did you approve this order? Were you aware that Davis Polk did, in fact, delete a sentence containing such a statement from one of AIG's SEC filings?[13] Do you now believe that it was appropriate for the FRBNY to order AIG not to disclose in its SEC filings that its counterparties received par value? If a member of the FRBNY legal staff had requested your approval to direct AIG to remove such statements from its SEC filings or from other communications, would you have approved?**

   I do not know whether the question correctly describes the events that occurred. But I had no role in making decisions regarding what to disclose about the specific financial terms of Maiden Lane III, the payments to AIG's counterparties, or AIG's securities filings. As cited above in the answers to Questions 1 and 2, information about these topics is generally available in the testimony before the Committee by Thomas Baxter, General Counsel of the Federal Reserve Bank of New York.

5. **When did you first become aware that members of Congress wanted to know the names of AIG's counterparties? [14] Was it appropriate for the FRBNY to resist the disclosure of the names of AIG's counterparties to Congress? [15] Was it appropriate for the FRBNY to resist the disclosure of the names of AIG's counterparties to the public?**

   I had no role in making decisions regarding what to disclose about the specific financial terms of Maiden Lane III and payments to AIGs counterparties. But I believe that the people involved are people of enormous integrity and experience. As discussed in the answer to

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[11] *See* FRBNY-TOWNS-R1-191773.
[12] *See* FRBNY-TOWNS-R1-005137.
[13] AIGHOGRM2200 (deletion of the following sentence from AIG's Form 8-K, filed Dec. 24, 2008: "As a result of this transaction, the AIGFP counterparties received 100 percent of the par value of the Multi-Sector CDOs sold and the related CDS have been terminated").
[14] *See* FRBNY-TOWNS-R1-139505 (Fed Congressional Liaison reports to FRBNY staff members on a Nov. 10, 2008 phone call with staff of the Senate Finance Committee and relays questions about the identities of AIG's counterparties).
[15] *See, e.g.,* FRBNY-TOWNS-R3-008604 ("Congress has enough information to assess what we did right now. They just want the counterparty names for purposes of political illustration...."); FRBNY-TOWNS-R3-011119 (FRBNY staff member speculates on the SEC's treatment of a filing by AIG: "Finally, even if we succeed in redacting the stuff we want to redact...this redacted information will still sit in the SEC's files, and the SEC may well get a request from Congress for that information. I don't know if there's a way to manage it so that Congress won't ask for it, or if they do, won't release it").

Questions 1 and 2 above, additional information related to these questions is available in the testimony before the Committee by Thomas Baxter, General Counsel of the Federal Reserve Bank of New York.

6. **Do you agree with FRBNY staff's request to the SEC that AIG's list of the assets Maiden Lane III had acquired, with counterparty names, transaction amounts, and securities identifiers, be treated in the same manner as "national security related files"?[16] If so, why was the information contained in the document so sensitive?**

   I had no role in making decisions regarding what to disclose about the specific financial terms of Maiden Lane III or the payments to AIGs counterparties. However, I believe that the people involved are people of enormous integrity and experience.

   I would point out that in 2008, circumstances for AIG were very different than they are today. The financial markets were much more fragile, and AIG was on the brink of potential collapse. As cited above in the answer to Questions 1 and 2, the testimony before the Committee by Thomas Baxter, General Counsel of the Federal Reserve Bank of New York, on January 27, 2010 provides additional information about these topics. Mr. Baxter stated: "[T]he New York Fed lawyers had two goals: (1) to help AIG make this filing accurate and consistent with the first; and (2) to protect, where appropriate, the substantial taxpayer funds at stake in Maiden Lane III" (Testimony, p. 15).

7. **Was it appropriate for the FRBNY to contact the SEC directly to argue that a portion of AIG's filings should be kept confidential and should not even be submitted to the SEC as part of its confidentiality determination? Or should the FRBNY have allowed AIG to conduct all communication with the SEC regarding its filings on its own?**

   I do not know whether the question as stated correctly describes the events that occurred. However, I had no role in making decisions regarding what to disclose about the specific financial terms of Maiden Lane III or the payments to AIGs counterparties. I believe that the people involved are people of enormous integrity and experience, and I trust that they acted appropriately under the circumstances.

8. **On March 16, 2009, AIG released selected information from Schedule A to the Shortfall Agreement between AIG and Maiden Lane III, including the names of its counterparties and aggregate pricing information for the purchases of underlying assets from the counterparties. Federal Reserve officials had warned that these disclosures would "undermine AIG's stability, the privacy and business interests of the counterparties, and the stability of the markets."[17] Do you agree that these warnings were wrong and that AIG's stability, the counterparties' interests, and the markets' stability were unaffected? Or do you believe that adverse consequences followed from AIG's March 16, 2009 disclosures?**

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[16] *See* FRBNY-TOWNS-R3-004119.

[17] Office of the Special Inspector General for the Troubled Asset Relief Program, *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Nov. 17, 2009, at 31.

I had no role in making decisions regarding what to disclose about the specific financial terms of Maiden Lane III or the payments to AIGs counterparties. However, I believe that the people involved are people of enormous integrity and experience, and I trust that they acted appropriately under the circumstances.

As discussed in the answer to Question 6 above, I would note that circumstances in March 2009 were very different than what they were during 2008. By March 2009, government assistance had succeeded in stabilizing AIG, and Maiden Lane III had completed the purchase of the securities from the counterparties. In addition, AIG had decided to wind down the AIG Financial Products derivatives business.

9. On January 27, 2010, the Committee on Oversight and Government Reform released the remaining information from Schedule A, including identifying information for each underlying asset that Maiden Lane III purchased from AIG's counterparties and the notional value, collateral posted, and negative mark-to-market associated with each individual transaction. What adverse consequences, if any, do you believe have resulted, or will result, from this disclosure?

We will never know the precise consequences of the decision, but it may make it harder for Maiden Lane III to sell those assets for their highest value. Ultimately, this would be to the detriment of U.S. taxpayers, who would otherwise have received those proceeds.

When information identifying individual securities in a portfolio and the individual prices paid for them is made available to traders in such securities, those traders are generally able to use that information to their advantage, at the expense of the owner of the securities. Private agents do not usually reveal such information for that reason.

10. On October 15, 2008, Sarah Dahlgren, an FRBNY Vice President, wrote you an e-mail message, reporting that "Board staff again reiterated that they didn't think that the Governors (unnamed) would go for ML2 or ML 3...they continue to push back hard on ML 3."18 What was the conflict between your staff at the FRBNY and the Federal Reserve Board staff in Washington regarding the planned establishment and transactions of Maiden Lane III? Why did the Federal Reserve Board eventually agree to go ahead with Maiden Lane III?

The creation of Maiden Lane II and III to purchase troubled assets that AIG had either acquired or insured was an important part of the assistance that the government provided to AIG to prevent it from failing. The Board of Governors of the Federal Reserve and the Federal Reserve Board of New York worked closely together in establishing these vehicles. We discussed different options before settling on the exact approach.

11. On November 17, 2008, AIG submitted a draft SEC filing to the New York Fed and Davis Polk for review, edits, and approval. The filing reported that a new compensation package had been signed by AIG's CFO, David Herzog. Within 40 minutes, Marshall Huebner, the lead partner for Davis Polk's FRBNY business, sent an

[18] FRBNY-TOWNS-R1-205129.

e-mail titled "READ ME" to Thomas Baxter, the FRBNY General Counsel. Huebner wrote, "Very bad timing to have this 8k come out just before the Secretary and the Chairman go before Waxman...Is there any chance—and maybe it is just too late—to get the Herzog comp package unagreed to?"[19] AIG never filed the SEC filing, and evidently canceled Herzog's compensation package. Were you consulted or informed about the FRBNY's actions in pressuring AIG to cancel the compensation package and not file the SEC filing? Did you approve these actions? If you were not consulted or informed, do you believe the FRBNY's actions in this matter were appropriate? Do you think avoiding embarrassment to the Fed and Treasury was a valid reason to cancel a required SEC filing?

Avoiding embarrassment is certainly not an appropriate reason for the government to take action. However, I do not know whether the question correctly describes the events that occurred. I lack the expertise to make a legal judgment about it, and I played no role in the decision referenced in your question. The e-mail cited in the question was sent to Thomas Baxter. I would refer you to his testimony before the Committee,[20] as well as the *Statement by the Federal Reserve Bank of New York Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*.[21]

12. **Do you believe that it is ever appropriate for the Fed, or Treasury, to force a public corporation that has received extraordinary federal financial assistance to make changes to its compensation arrangements, or take other actions, in order to avoid making disclosures under the securities laws? When are such actions appropriate?**

Compensation arrangements at firms that received financial assistance from the government during the financial crisis have been the subject of much debate and controversy. The broad questions defy a simple, generalized response. However, I believe that transparency about the decisions that are actually made is very important.

In the case of AIG's actions in 2008, the Federal Reserve Bank of New York addressed the issues in its *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III* in January. In particular, the FRBNY stated: "AIG at all times remained responsible for complying with its disclosure obligations under the securities laws and, during the period at issue, AIG devoted substantial resources to fulfilling its disclosure obligations, including obtaining expert legal advice from the experienced outside law firms of Sullivan & Cromwell LLP and Weil Gotshal & Manges LLP. The role of the FRBNY and its counsel in communicating with AIG regarding the securities disclosures associated with the transaction did not supplant the decision making of AIG and its counsel with respect to AIG's legally required disclosures. Rather, the role of the FRBNY and its counsel was (1) to work with AIG to further the goals of accuracy and consistency of AIG's filings with respect to the transactions, and (2) to protect, where appropriate, the substantial taxpayer funds at stake in

[19] FRBNY-TOWNS-R3-002270
[20] Thomas C. Baxter Jr., *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Testimony before the Committee on Government Oversight and Reform, January 27, 2010.
[21] Federal Reserve Bank of New York, *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, January 19, 2010, *available* at http://www.newyorkfed.org/markets/st100119.html.

Maiden Lane III. In the end, after receiving the FRBNY's suggestions, AIG, aided by its internal and outside attorneys, made the disclosures that it deemed to be legally required and otherwise appropriate."[22]

13. AIG and the New York Fed created Maiden Lane III on November 25, 2008. Sarah Dahlgren, a Senior Vice President at the New York Fed in charge of the New York Fed's dealings with AIG, told Davis Polk that she did not want AIG to report the transactions to the SEC that day, saying in an email that "I really don't want the ML III to go out today...is the company still aiming to try to issue this today?..." Ethan James, a Davis Polk partner, responded to her email saying "we gotcha covered. You only need hear Kathy's pathetic voicemail to understand how well trained she is-at least for now!"[23] Is it appropriate for a federal government agency to browbeat and control a financial disclosure officer of a public company to the point where she is "well trained?" Is it appropriate for the federal government to dictate the timing of a public company's securities filings solely for its own convenience?

I played no role in the decisions referenced in your question. However, the Federal Reserve Bank of New York addresses this question in its *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III*, cited above in the response to Question 12. In particular, the Statement notes: "a lawyer for the FRBNY asked a lawyer at AIG if it would be feasible to hold off on the filing of the 8-K and the related press release until the following week in order to allow the FRBNY sufficient time to review the proposed filings and to make a contemporaneous FRBNY informational release. The FRBNY and AIG agreed that the rules of the Securities and Exchange Commission ("SEC") provided the company until Tuesday of the following week (December 2, 2008) to file the 8-K. The filing was timely made on December 2."

14. One failure of the financial regulatory system that led to the current recession was the inability of the various regulatory entities to effectively share information. In addition, there seems to have been a lack of predictive analysis to identify weaknesses before they became failures. How are the Treasury Department and other regulatory agencies, such as OCC and FDIC, working proactively to improve coordination with each other – or even between the divisions of the individual agencies themselves – and what improvements in predictive analysis have been made so that there is an ability to provide the holistic view necessary to prevent future economic crises?

The Department of Treasury chairs the President's Working Group on Financial Markets (PWG) and has been actively working through that body and through informal relationships with regulators to improve coordination on critical issues for financial markets.

Recently, the interagency collaborations have resulted in joint statements and aligned efforts on both commercial real estate and small business lending – reflecting the critical importance of consistent efforts in those areas for our financial system and economy.

[22] Federal Reserve Bank of New York, *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, January 19, 2010, *available* at http://www.newyorkfed.org/markets/st100119.html.
[23] FRBNY-TOWNS-R1-030952.

In addition, the Administration has proposed to create a Financial Services Oversight Council (FSOC) with explicit information gathering authority and a duty to report to Congress each year on emerging threats to the financial system. I commend the Members of this Committee for advancing financial reform to this point, and I look forward to continuing to work with you to enact a strong set of comprehensive reforms.

Rep. Dan Burton

1. **During your tenure as President of the Federal Reserve Bank of New York, to what degree were you involved in the negotiations with AIG's counterparties to determine the price that would be paid for the underlying assets?**

   I was not personally involved in the negotiations with the counterparties, which were conducted by my colleagues at the Bank. However, they kept me apprised of the progress of the negotiations during early November. I described the circumstances of the negotiations in detail in my testimony before the Committee in January.

2. **After the Federal Reserve Board authorized the Federal Reserve Bank of New York to lend up to \$85 billion to AIG to enable AIG to avoid bankruptcy, how much of your time was consumed by AIG-related matters?**

   AIG occupied a significant amount of my time, but we were also working simultaneously to respond to many other aspects of the financial crisis during that period. We were facing escalating challenges on many fronts. For example, Lehman Brothers filed for bankruptcy just a few days after AIG alerted Federal authorities that its problems had become acute. In the wake of Lehman's failure, major institutions such as Washington Mutual and Wachovia experienced debilitating deposit withdrawals. Money market funds also suffered a broad run, threatening what was considered one of the safest investments for Americans and severely disrupting the commercial paper market, a vital source of funding for many businesses.

3. **You have stated that you were not a party to the discussions regarding AIG's filings with the Securities and Exchange Commission as those discussions occurred after your nomination to be U.S. Treasury Secretary and you had recused yourself from all Federal Reserve business. You were officially announced as the President-Elect's nominee on November 25, 2008. One of the e-mails subpoenaed by the Committee, dated November 11, 2008, quotes a Federal Reserve Bank official: "As a matter of course, we do not want to disclose that the concession is at par unless absolutely necessary."[24]**

   a. **Since this e-mail was sent a full 14 days before your nomination as Treasury Secretary is it still your contention that you were completely unaware of any discussion between the Federal Reserve Bank of New York and AIG to hide the details of the AIG counterparties' deal from the American public?**

      I had no role in making decisions about AIG's securities filings, before or after my nomination. Also, it is important to clarify the precise scope of my recusal after President-elect Barack Obama announced that he intended to nominate me to be Secretary of the Treasury. I did not recuse myself from all Federal Reserve business.

[24] *See* FRBNY-TOWNS-R1-191773.

Specifically, starting on November 24, 2008, I withdrew from involvement in monetary policy decisions, policies involving individual institutions, as well as day-to-day management activities.

b. Can you produce a copy of your notice of recusal for the record?

There is not a physical document to this effect. After conferring with the Chairman of the Federal Reserve and the General Counsel of the Federal Reserve Bank of New York, among others, I notified my colleagues and staff about my decision to withdraw from day-to-day management activities and decisions involving individual institutions. They understood that I would not be working on any bank supervision matters or related issues.

c. As a key figure in the scenario, and as the potential future Treasury Secretary, even if you were not a party to the discussion, why didn't you insist that you be fully informed on all matters related to AIG's bailout?

At this point in the crisis, a near-complete collapse of our financial system was a realistic possibility. Lehman Brothers filed for bankruptcy just a few days after AIG alerted Federal authorities that its problems had become acute.

In the wake of Lehman's failure, major institutions such as Washington Mutual and Wachovia experienced debilitating deposit withdrawals, eventually collapsed, and were acquired by competitors. Money market funds also suffered a broad run, threatening what was considered one of the safest investments for Americans and severely disrupting the commercial paper market, a vital source of funding for many businesses. I was working hard to address all aspects of the crisis. Given the scope of events, prior to my nomination, I stayed involved in key policy decisions about AIG, but I was not involved with every issue that arose related to it. The leadership team and staff at the Federal Reserve Bank of New York all worked together to address the crisis.

d. If you were excluded from the day-to-day operations of the Federal Reserve Bank of New York during the time period, who was making decisions to conceal information from the taxpayers about how their money was being mis-spent, and when will they be held accountable?

I do not agree with the characterizations in the question. We acted because the consequences of AIG failing at that time, in those circumstances, would have been catastrophic for our economy and for American families and businesses. In designing and implementing the transactions, the main objective was to get the best deal for the U.S. taxpayer. The people who worked with me are dedicated and talented public servants. I believe that they acted with the highest integrity during a time of tremendous stress and uncertainty.

4. **Since the beginning of 2009, the Obama Administration has exercised an unprecedented amount of control over the American automotive industry. Some believe this control has resulted in the picking of winners and losers among those retirees who have been impacted by auto bankruptcies. A review of the Master Disposition Agreement General Motors filed with the bankruptcy court Southern District of New York clearly indicates that "any GM contributions under a PBGC Agreement will be subject to U.S. Treasury consent."**

   a. **What role did the Treasury Department play in the decision to terminate the pension plan of the Delphi Salaried workers?**

   The decision to terminate Delphi's pension plans was initiated by the PBGC and agreed to by Delphi as part of a settlement agreement. Treasury did not make this decision.

   The termination of the Delphi Retirement Program for Salaried Employees and its placement under the PBGC's trusteeship are currently the subject of litigation in Black et al. v. PBGC et al. in Michigan. I cannot comment on the specifics of any pending litigation. For your information, I have enclosed a copy of the brief filed by Treasury and other defendants on February 16, 2010 in *Black*.

   In addition, I would note that the PBGC Board, via the Board Representatives, is regularly advised of probable terminations for accounting purposes, and PBGC's actions affecting companies. The Board has been advised regularly about matters involving Delphi, the impact on PBGC, plan participants and benefit cutbacks. I note, however, that the PBGC Board does not make individual case decisions; rather it is advised of significant matters and consulted about them, but case decisions lie solely with the PBGC Director.

   With regards to the government's broader efforts to assist the auto industry, I would note that on December 19, 2008 President Bush announced that, in the absence of alternative aid measures from the Congress, he would use authority provided by the Congress under the Emergency Economic Stability Act (EESA) to make available capital to assist the domestic auto industry in becoming financially viable, to facilitate the restructuring of the domestic auto industry, and to prevent disorderly bankruptcies during a time of economic difficulty.[1] The initial loans to GM and Chrysler closed on December 31, 2008 and January 2, 2009, respectively.

   b. **Did the Treasury Department participate in discussions with the Pension Benefit Guaranty Corporation about the termination of Delphi Salaried workers' pension plan?**

   Please refer to response to 4a. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

[1] White House Office of the Press Secretary, *Fact Sheet: Financing Assistance to Facilitate the Restructuring of Auto Manufacturers to Attain Financial Viability* (Dec. 19, 2008) (online at georgewbushwhitehouse.archives.gov/news/releases/2008/12/20081219-6.html).

c. **If so, what was the position of the Treasury Department in those discussions and the reasoning behind any decision to force only the Delphi Salaried workers to undergo substantial cuts in their pensions?**

Please refer to response to 4a. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

d. **Is the Treasury Department willing to publicly release all records and communications between the U.S. Department of Treasury and the President's Automotive Task Force, the United Auto Workers, the Pension Benefit Guaranty Corporation, General Motors, Delphi Corporation and Holding, and any Member of Congress or other public official, referring or relating to retirement or pension benefits for General Motors or Delphi Corporation employees, between November 1, 2008, and November 1, 2009?**

Please refer to response to 4a. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

5. **The United Auto Workers, which represents Delphi Hourly Retirees, has stated that Delphi Salaried Retirees should be treated with fairness and equity. In other words, the UAW supports providing the same "top-ups" to the salaried workers that were provided to the other Delphi workers. Does the Administration agree?**

As you may know, the question of pension "top-ups" for certain Delphi retirees is currently the subject of litigation in *Black et al. v. PBGC et al.* in Michigan. I cannot comment on the specifics of any pending litigation. For your information, enclosed is a copy of the brief filed by Treasury and other defendants on February 16, 2010, in *Black*.

a. **If so, what steps is the Administration taking or planning to take as the majority owner of General Motors to implement "top-ups" for the salaried workers?**

Please refer to response to 4a. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

b. **If not, what is the Administration's justification for continuing to treat these two groups differently?**

Please refer to response to 4a. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

6. **During the hearing I briefly touched upon the question of Representative Ron Paul's "Federal Reserve Transparency Act of 2009" (H.R. 1207), which requires a General Accountability Office audit of the Board of Governors of the Federal Reserve System and the Federal Reserve banks before the end of 2010. The bill is current co-sponsored by 317 Members of the House of Representatives, significantly more than 2/3rds of the total membership of the House. Does the Administration support this legislation to bring more transparency to the operations of the Federal Reserve?**

a. **If so, is the Administration prepared to work with House and Senate Leadership to schedule a vote on this legislation before the congressional recess in April?**

   Please refer to response to 6b.

b. **If not, why?**

   The Federal Reserve is subject to audits by the GAO across a wide range of its responsibilities. All of its supervisory and regulatory functions are subject to audit by the GAO to the same extent as the supervisory and regulatory functions of the other federal banking agencies. In addition, the GAO has conducted audits of the Federal Reserve in a wide range of other areas, including its oversight and operation of payment systems; its implementation and enforcement of consumer protection laws; its policies on the acquisition of U.S. banking organizations by sovereign wealth funds; its efforts to address cyber security; and the need for financial regulatory reform.

   The Congress purposefully--and for good reason--chose to exclude from GAO review only two highly sensitive areas: one is monetary policy deliberations, decisions, and actions, including open market and discount window operations; and the other is Federal Reserve transactions for or with foreign central banks, foreign governments, and public international financing organizations.

   Considerable experience shows that monetary policy independence--within a framework of legislatively established objectives and public accountability--tends to yield a monetary policy that best promotes price stability and economic growth. Monetary policy independence prevents governments from succumbing to the temptation to use the central bank to fund budget deficits.

   It also enables policymakers to look beyond the short term as they weigh the effects of their monetary policy actions on price stability and employment. And it reinforces public confidence that monetary policy will be guided solely by the objectives laid out in the Federal Reserve Act. Thus, the Congress has sought to maintain an independent monetary policy not because it benefits the Federal Reserve, but because of the important public benefits it provides.

7. **I have spoken to a number of financial managers about the President's financial reform proposal, and they understandably expressed some serious concerns. So far as I am aware, hedge funds, private equity and proprietary trading were not root causes of the current economic crisis. Can you clarify how the President's proposal would do anything other than limit the competitiveness of American financial companies, particularly in light of the fact that most governments, particularly European governments, have signaled that they are unwilling to pursue similar regulatory reforms?**

   We do not believe that these proposals will adversely impact the competitiveness of U.S. firms. Major financial firms in other economies already operate with fewer restrictions on their activities than do U.S. banking firms. Yet, the more limited activities of U.S. banking firms have not materially impaired the capacity of U.S. firms to compete in global financial markets against foreign universal banks, nor have these variations stopped the United States from being the leading financial market in the world.

8. **A key lesson that should be learned from the current economic crisis is that companies should be overseen based on the activity they engage in rather than allowing them to choose who they want to be regulated by. Yet, the Administration's proposal seems to create a system that picks and chooses financial companies that will be allowed to drop their status as bank holding companies in order to avoid regulations that would be imposed on other parts of the industry. This seems like a glaring loophole and a fundamental flaw in the President's proposal that would encourage regulatory arbitrage. Do you agree that this loophole exists? If so, are you concerned about its effects and have you thought of ways to fix it?**

   I do not agree that a loophole exists. The purpose of the Administration's proposal is to separate the subsidy of federally insured deposits from risky activities that are unrelated to a customer. But it does not let major firms escape tough supervision and oversight. Under our regulatory reform proposals, all major financial firms, regardless of whether they own a depository institution, must be subject to robust consolidated supervision and regulation (including strong capital and liquidity requirements) by the federal government.

   Moreover, our proposal would apply to any firm that controls an insured depository – not just depository institutions that are banks and not just to bank holding companies. This is consistent with the Administration's proposal in the broader reform package to shut down the loopholes in the Bank Holding Company Act.

   Finally, the legislative proposal we delivered to Congress would specifically require the Federal Reserve to impose additional capital requirements and quantitative limits on the proprietary trading and hedge fund and private equity activities of non-bank financial firms that could pose a threat to financial stability.

9. **I understand that you have concerns about the President's proposal. Can you elaborate on those concerns?**

   I fully support the President's proposal.

Rep. Mark Souder

1. **In its negotiations with AIG's counterparties, why did the FRBNY elect not to factor in the substantial differences in the financial position of the respective counterparties, including their exposure to AIG securities, benefits they may have received from other government programs such as TARP, and the fact that some of the institutions were foreign owned? If you were not directly involved with this decision, do you agree with this policy choice? Did the decision to treat all counterparties the same essentially eliminate any possibility to negotiate concessions?**

   Due to the nature of the contracts that AIG had entered into when selling insurance on the troubled securities, the contractual rights of the counterparties were very well protected. The counterparties had purchased insurance from AIG that entitled them, as a matter of law, to the full or par value of the contracts.

   The financial health of individual counterparties was not a consideration in the rescue of AIG. All of the counterparties were treated the same. If the government had tried to force individual counterparties to take a concession on the value of their contracts based on their financial strength, it would have been forcing private firms to forfeit contractual rights for the benefit of another financial institution. That would have violated private parties' contractual rights and undermined confidence in the government's overall efforts to stabilize the U.S. financial system.

Rep. Michael R. Turner

1. **The administrative record produced by the Pension Benefit Guaranty Corporation ("PBGC") indicates that PBGC staff discussed the Delphi pension plans with officials from the Treasury Department and the Auto Task Force before the plan was finalized to cut the pension plans. At what date did the Treasury Department know about the cuts to the Delphi pension plans?**

   The termination of the Delphi Retirement Program for Salaried Employees and its placement under the PBGC's trusteeship are currently the subject of litigation in Black et al. v. PBGC et al. in Michigan. I cannot comment on the specifics of any pending litigation. For your information, I have enclosed a copy of the brief filed by Treasury and other defendants on February 16, 2010 in *Black*.

   In addition, I would note that the PBGC Board, via the Board Representatives, is regularly advised of probable terminations for accounting purposes, and PBGC's actions affecting companies. The Board has been advised regularly about matters involving Delphi, the impact on PBGC, plan participants and benefit cutbacks. I note, however, that the PBGC Board does not make individual case decisions; rather it is advised of significant matters and consulted about them, but case decisions lie solely with the PBGC Director.

   With regards to the government's broader efforts to assist the auto industry, I would note that on December 19, 2008 President Bush announced that, in the absence of alternative aid measures from the Congress, he would use authority provided by the Congress under the Emergency Economic Stability Act (EESA) to make available capital to assist the domestic auto industry in becoming financially viable, to facilitate the restructuring of the domestic auto industry, and to prevent disorderly bankruptcies during a time of economic difficulty.[1] The initial loans to GM and Chrysler closed on December 31, 2008 and January 2, 2009, respectively.

2. **In what manner was the Treasury informed about the cuts to the Delphi Salaried Retiree pension plans?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

3. **Does the Treasury Department acknowledge that they knew about the Delphi Salaried Retiree pension cuts prior to final administrative action from PBGC to implement any cuts to those pensions?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

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[1] White House Office of the Press Secretary, *Fact Sheet: Financing Assistance to Facilitate the Restructuring of Auto Manufacturers to Attain Financial Viability* (Dec. 19, 2008) (online at georgewbushwhitehouse.archives.gov/news/releases/2008/12/20081219-6.html).

4. **With what frequency did these discussions occur, and at what level?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

5. **Did the Treasury Department initiate the discussions with the PBGC regarding the Delphi Salaried Pension plans?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

6. **Is the Treasury Department consulted in PBGC pension fund plan settlement negotiations?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

7. **Did the Treasury Department authorize, approve, or consent to the PBGC terminating the Delphi Salaried workers pension plans?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

8. **Does the Treasury Department deny it had the authority to disapprove of the cuts to the Delphi Salaried Retiree pension plans?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

9. **What authority does the Department of the Treasury have to prevent the cuts to the Delphi Salaried Retiree pension plans?**

   Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

10. **In the discourse between the Treasury, the PBGC and any other parties, what role did the Treasury Department play in the decision to terminate the pension plan of the Delphi Salaried workers?**

    Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

11. **What was the position of the Treasury Department in any of those discussions and the reasoning behind any decision to force only the Delphi Salaried workers to undergo substantial cuts in their pensions?**

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

12. Recently, it was decided that certain hourly retirees and other union workers whose pensions were cut by the PBGC would have those pensions "topped-up" by the new OM. What role did the Treasury Department have in that decision?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

13. How much is the "topping-up" costing New GM?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

14. The Secretary of the Treasury sits as one of three board members of the PBGC. Did the Secretary of the Treasury take any action to prevent the cuts to the Delphi Salaried Retiree pension plans?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

15. The Secretary of the Treasury sits as one of three board members of the PBGC. Did the Secretary affirmatively consent and/or approve of cuts to the Delphi Salaried Retiree pension plans?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

16. The Secretary of the Treasury sits as one of three board members of the PBGC. Why did the Secretary not exercise any authority to prevent the cuts to the Delphi Salaried Retiree pension plans?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

17. Did the PBGC vote on the cuts to these plans, and what was the Treasury Secretary's vote?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

18. The Secretary of the Treasury sits as one of three PBGC board members. What does the Secretary see as his responsibilities to the PBGC as a board member?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

19. Please describe the actual conflicts and potential conflicts between the Secretary's duties as a PBGC board member and the Treasury Department's duties as the majority owner of New GM?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

20. How does the Secretary prevent conflicts between those two roles?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

21. After the Treasury Department's increased involvement in General Motor's operations, General Motors seemed to reverse its position with respect to assuming the obligations of Delphi's pension plan for salaried workers. Please describe the role of the Treasury Department in that decision?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

22. Please provide and describe any communications between the Treasury Department and General Motors with respect to General Motors' position of assuming the obligations of Delphi's pension plan for salaried workers.

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

23. By the time the PBGC initiated termination proceedings against Delphi's pension plans, the PBGC held approximately $200 million in liens against Delphi foreign assets, and estimated that there were approximately $2.4 billion in Delphi foreign assets that the PBGC could potentially assert liens against. The PBGC ultimately released these liens as part of settlement agreements with New GM and Delphi, in exchange for payments by New GM which did not include Delphi Salaried Retirees pension plans. What role did the Treasury Department play in approving and or crafting this settlement?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

24. When did the Treasury Department become aware that the PBGC believed that there were $2.4 billion in foreign Delphi assets upon which the PBGC could assert liens?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

25. Had the PBGC refused to remove the liens, would the Treasury Department have been willing to permit New GM to assume sponsorship of the salaried pension plan?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

26. Did the Treasury Department (or the Auto Task Force) take part in negotiations with the PBGC in an attempt to have the PBGC release its liens against Delphi Assets? And in what manner?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

27. When the Treasury Department communicated with the PBGC regarding the negotiation of a settlement agreement and the release of the PBGC's liens, did the Treasury Department take any measures to ensure that the PBGC would not give undue weight to the negotiation position of GM and or the Treasury Department due to political considerations?

Please refer to our response to Question No. 1. As discussed, I cannot comment specifically on these topics as they are the subject of pending litigation.

28. Salaried Delphi retirees have made requests under the Freedom of Information Act to the Treasury Department and the Auto Task Force, respectively, regarding their involvement in the termination of the salaried pension plan. These requests have so far been ignored. Can you explain why the Treasury Department and Auto Task Force have refused to comply with these requests?

I apologize for the delay. Treasury has a first-in, first-out policy in responding to FOIA requests. Treasury personnel are working to respond to pending requests in a manner consistent with department regulations.

29. Members of the House Oversight and Government Reform Committee, as well as other House Members have requested documentation related to the Treasury Department's knowledge and role in the cuts to the Delphi Salaried Retiree pension plans. These requests have so far been ignored. Please explain the Department's reasoning behind ignoring Congressional requests for information, and please describe when the Department will provide the requested information to the Members of Congress.

I apologize for the delay. Treasury personnel are working to respond to pending requests in a manner consistent with department regulations.

30. The United Auto Workers has recently stated that Delphi Salaried Retirees should be treated with "fairness and equity". Additionally, the UAW stated in a letter dated January 15, 2010 that it supports providing the same "top-ups" to the Salaried workers

as a matter of "fairness and equity" that were provided to the other Delphi workers. Does the Administration agree?

As you may know, the question of pension "top-ups" for certain Delphi retirees is currently the subject of litigation in *Black et al. v. PBGC et al.* in Michigan. I cannot comment on the specifics of any pending litigation. For your information, I have enclosed a copy of the brief filed by Treasury and other defendants on February 16, 2010 in *Black.*

Rep. Lynn A. Westmoreland

1. **Once the Government took over 79% of AIG, it was Government-owned. Why did the FRBNY not insist that the Government's Triple-A rating be extended to AIG to ease AIG's collateral posting obligations under its CDS contracts?**

   AIG remains a private company, run by private management, and overseen by an independent board of directors. Neither the company nor its obligations are guaranteed by the full faith and credit of the federal government or the Federal Reserve.

   The liquidity that Treasury and FRBNY have provided has helped stabilize AIG and lowered the risk of default. But the government's commitment to AIG has always been limited and subject to the terms of the commitments expressed.

   In terms of influencing AIG's credit rating, the Federal Reserve Bank of New York does not have the authority to tell private credit rating agencies how to evaluate individual companies. The rating agencies are a proxy for how the market views AIG's creditworthiness. It is important that those views to be formed independently, not according to the will of a public agency.

2. **It is obvious that the AIG deal is bad for taxpayers and that if the deal is not renegotiated taxpayers will never see their money get repaid. Is there anybody at Treasury working on a new plan to deal with AIG?**

   I respectfully disagree with the assertion that the rescue of AIG was a bad idea for taxpayers. The goal of the government intervention was to prevent AIG's collapse and maintain the continuous operations of its insurance businesses. AIG was the largest provider of conventional insurance in the world. The rescue plan succeeded in keeping them operational and averting the catastrophic consequences for taxpayers that would have resulted from AIG's failure. Treasury staff worked hard on the rescue of AIG, and we continue to do so.

   The U.S. government is still exposed to substantial risk of losses on its investments in AIG. As I discussed in my testimony before the Committee, that risk was unavoidable, and we cannot know at this point what the scale of those losses will be. But, on the basis of a range of measures, those losses are likely to be lower than we expected even just a few months ago.

   Today, AIG's insurance operations are open for business and generating positive returns. In addition, the Federal Reserve will likely be repaid in full and earn a positive return on its financial support of AIG, including the FRBNY Credit Facility, its loans to Maiden Lane II and Maiden Lane III, and its preferred interests in AIA Aurora and ALICO Holdings. AIG recently announced that it reached agreements to sell those two international subsidiaries for a total of more than $50 billion. Much of the profit will be used to pay back part of the Federal Reserve's loan and redeem its preferred interests.

Rep. Patrick McHenry

1. **In a hearing before the Financial Services Committee last year, you said: "Financial products and institutions should be regulated for the economic function they provide and the risks they present, not the legal form they take. We can't allow institutions to cherry pick among competing regulators and ship risk to where it faces the lowest standards and weakest constraints." You suggested that you could "reconcile" this view with current financial regulation proposals, which would allow some companies to avoid regulation by dropping their status as a bank holding company. Please explain.**

   I do not agree that a loophole exists. The purpose of the Administration's proposal is to separate the subsidy of federally insured deposits from risky activities that are unrelated to a customer. But it does not let major firms escape tough supervision and oversight. Under our regulatory reform proposals, all major financial firms, regardless of whether they own a depository institution, must be subject to robust consolidated supervision and regulation (including strong capital and liquidity requirements) by the federal government.

   Moreover, our proposal would apply to any firm that controls an insured depository – not just depository institutions that are banks and not just to bank holding companies. This is consistent with the Administration's proposal in the broader reform package to shut down the loopholes in the Bank Holding Company Act.

   Finally, the legislative proposal we delivered to Congress would specifically require the Federal Reserve to impose additional capital requirements and quantitative limits on the proprietary trading and hedge fund and private equity activities of non-bank financial firms that could pose a threat to financial stability.

2. **Please elaborate on President Obama's proposed tax on banks. Do you believe it will result in less credit being made available to small businesses and consumers?**

   In reality, the firms that are subject to the fee have a competitive incentive not to pass on costs. The vast majority of their competitors – including all firms with less than $50 billion in assets – will not face the fee, so trying to increase costs to their customers will likely result in lost market share.

3. **How do you think proposed limits on hedge funds, private equity, and proprietary trading will impact U.S. firms' global competitiveness?**

   We do not believe that these proposals will adversely impact the competitiveness of U.S. firms. Major financial firms in other economies already operate with fewer restrictions on their activities than do U.S. banking firms. Yet, the more limited activities of U.S. banking firms have not materially impaired the capacity of U.S. firms to compete in global financial markets against foreign universal banks, nor have these variations stopped the United States from being the leading financial market in the world.

Rep. Jim Jordan

1. **Do you believe that the management team that the FRBNY put in place at AIG was qualified to run an insurance company? Please describe the relevant experience and qualifications of each FRBNY employee who was given any AIG management responsibilities on or after September 18, 2008.**

   AIG remains a private entity, run by private management, and overseen by an independent Board of Directors. In its efforts to stabilize and restructure the company, the Federal Reserve has acted as a lender to AIG. To my knowledge, no Federal Reserve employee has ever been given operational management responsibilities at AIG.

   In designing our intervention, the government made sure that there were appropriately tough conditions that put the burden of failure on AIG's existing equity holders and management and started the process of designing a comprehensive restructuring plan.

   The Federal Reserve extended AIG a line of credit on September 16, 2008. When AIG accepted it, the Government required AIG's then-CEO to step down immediately. In his place, Edward Liddy, the former chairman, president and CEO of Allstate Corporation agreed to serve as AIG's CEO for a salary of $1 per year to help assist the company in its restructuring and recovery. Today, Robert Benmosche serves as CEO. Previously, he served as Chairman and CEO of MetLife, Inc.

2. **In an e-mail to you on October 22, 2008, Meg McConnell, a FRBNY economist, noted that "the new ML 3-in which they tear up the CDS and purchase the underlying CDOs-seems pretty good from a financial stability perspective...[because] it seems to remove considerably more uncertainty for the firms and arguably for the system."[25] Did the FRBNY consider the financial health, or stability, of AIG's counterparties in deciding how to structure and conduct the Maiden Lane III transactions?**

   The financial health of individual counterparties was not a consideration in the rescue of AIG. All of the counterparties were treated the same. The prices paid for the securities were their fair market value, and because the counterparties retained the collateral they had previously received from AIG, they all received an aggregate amount equal to par value of their securities. In return, the insurance contracts were terminated, and the counterparties transferred the securities to Maiden Lane III.

3. **Do you agree with FRBNY staff's position that a "governmental interest" justified special treatment by the SEC for AIG's filings, distinct from the filings of all other companies?[26] If so, please describe that "governmental interest." Is the "governmental interest" distinct from the policy goals of the securities disclosure laws and rules?**

   I was not involved in making decisions about AIG's securities filings, nor do I have the expertise to make that legal judgment. For a detailed discussion of those topics, I would refer

[25] FRBNY-TOWNS-R1-195645.
[26] *See* FRBNY-TOWNS-R3-009189.

you to the testimony before the Committee by Thomas Baxter, General Counsel of the Federal Reserve Bank of New York,[27] as well as the *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, dated January 19, 2010.[28]

[27] Thomas C. Baxter Jr., *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Testimony before the Committee on Government Oversight and Reform, January 27, 2010.
[28] Federal Reserve Bank of New York, *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, January 19, 2010, *available* at http://www.newyorkfed.org/markets/st100119.html.

Rep. Blaine Luetkemeyer

1. **Why did the FRBNY reject less costly alternatives to acquiring the underlying assets from AIG's counterparties and seeing that they received the full $62 billion up front, such as stepping in to provide collateral to the counterparties as needed under the CDS contracts? If you felt that you did not have the necessary statutory authority, why did you not come to Congress and ask for it?**

   From the beginning, it was clear that AIG needed a durable restructuring of its balance sheet and operations. The credit provided by the Federal Reserve on September 16th stemmed the bleeding by satisfying AIG's immediate liquidity needs, but that was not enough. The problems at AIG were so deep that they required a more permanent restructuring.

   In designing and implementing the transactions to purchase the securities our primary objective was, as it always is, to get the best result for the taxpayer. We made judgments about these transactions carefully with the advice of outside counsel and financial experts. In the end, the prices paid for the securities were their fair market value. Because of the way the contracts worked, those prices were essentially equal to the difference between the par value of the CDOs and the payments that counterparties had already received.

   I join the American people and Members of Congress in feeling a deep sense of outrage over this crisis, and over the fact that better tools were not available for the government to confront it. For that reason, we should put in place a set of financial reforms that would create a safer, more stable financial system, where opportunity can rise, risk can be mitigated, and where there are stronger protections for consumers, investors, and taxpayers.

2. **FRBNY General Counsel Thomas Baxter, when asked about the FRBNY's negotiations with AIG's counterparties, told Committee staff, "I don't know why we even bothered to ask [for any concessions]." When he was asked why, he responded, "I guess it doesn't hurt to ask." Why was such a limited effort made to seek concessions from the counterparties?**

   We had very little negotiating leverage. The counterparties were in a very strong position and generally protected in the event of AIG's default. They held insurance contracts entitling them to full or par value of the contracts. If AIG had defaulted, or even filed for bankruptcy, the counterparties would have kept both the cash collateral payments that they had previously received from AIG as well as the underlying securities.

   In addition, AIG's financial position was deteriorating rapidly and the prospect of a downgrade by the credit rating agencies was imminent. As I discussed in my Testimony before the Committee, we had to act very quickly. Not unexpectedly, we discovered that most firms would not, under any condition, provide a concession.

3. **In 2008 and 2009, the FRBNY and its counsel shared AIG's draft SEC filings with officials at Treasury and requested comments and edits. When a corporation's securities disclosures become a group project of multiple federal agencies, with each agency adding changes to suit its own needs, is there a danger that investors' needs will be ignored?**

   I was not involved in any decisions regarding AIG's securities filings. But I know that the Federal Reserve Bank of New York staff who were involved are people of enormous integrity and experience. I trust that they acted appropriately under the circumstances.

   For more information about the topic, I would refer you to the testimony before the Committee by Thomas Baxter, General Counsel of the Federal Reserve Bank of New York,[29] as well as the *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, dated January 19, 2010.[30]

4. **You have repeatedly claimed that the Fed will actually make a profit from the AIG bailout. Can you provide any concrete proof of your claims?**

   The U.S. government is still exposed to substantial risk of losses on its overall investments in AIG. That risk was unavoidable, and we cannot know at this point what the exact scale of those losses will be.

   The Federal Reserve will likely be repaid in full and earn a positive return on its financial support of AIG, including the FRBNY Credit Facility, its loans to Maiden Lane II and Maiden Lane III, and its preferred interests in AIA Aurora and ALICO Holdings. AIG recently announced that it reached agreements to sell those two international subsidiaries for a total of more than $50 billion. Much of the profit will be used to pay back part of the Federal Reserve's loan and redeem its preferred interests.

   Further, as I discussed in response to Question 1 above, since Maiden Lane III purchased the securities from the counterparties, they have generated significant cash flows that have been used to pay down the Federal Reserve's loan by more than 25 percent, and the value of the remaining portfolio significantly exceeds the outstanding loan balance and accrued interest on the loan. Similarly, cash flows from Maiden Lane II have already been used to pay down the Federal Reserve's loan by roughly 25 percent, and remaining portfolio holdings of Maiden Lane II exceed the outstanding loan balance and deferred interest on the loan.

   Unfortunately, TARP investments in AIG will likely still result in some loss. But today, Treasury believes that the losses are likely to be lower than was thought even a few months ago.[31]

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[29] Thomas C. Baxter Jr., *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Testimony before the Committee on Government Oversight and Reform, January 27, 2010.
[30] Federal Reserve Bank of New York, *Statement Regarding Public Disclosures of AIG Concerning Maiden Lane III LLC*, January 19, 2010, *available* at http://www.newyorkfed.org/markets/st100119.html.
[31] Congressional Budget Office, Report on the Troubled Asset Relief Program, Mar. 2010, at 3-4, *available at* http://www.cbo.gov/ftpdocs/112xx/doc11227/03-17-TARP.pdf.

Rep. Stearns, Participating by Unanimous Consent of the Committee

1. **It was brought out in your testimony and through the questions that were asked by the Members of the House Oversight and Government Reform Committee at the January 27th hearing that you did not sign an official, formal agreement to recuse yourself from the dealings and decisions involving the overpayments to AIG's counterparties and from working on issues involving specific companies, including AIG. Because you only informally recused yourself, American taxpayers and Congress have to trust you and take you at your word that you did not get involved with "issues involving specific companies, including AIG" following your nomination for Treasury Secretary on November 24, 2008. Is that true? Please respond with either "yes" or "no".**

   I am not aware of any legal reason that would have made it necessary for me to stop conducting my duties as President. The decision to withdraw from certain activities was made, out of an abundance of caution, in part to protect the independence of the Federal Reserve Bank of New York, and, in part, because of the time demands that I was going to face in helping to shape the President-elect's economic strategy. Specifically, starting on November 24, 2008, I withdrew from involvement in monetary policy decisions, policies involving individual institutions (including AIG), and day-to-day management activities.

   I conferred with the General Counsel of the Federal Reserve Bank of New York, among others, about the decision to stay on as President on an interim basis, as well as my withdrawal from certain activities. My colleagues and staff were aware of this decision. I am not aware of any requirement to confirm such a recusal in writing.

2. **What was the rationale behind your decision to only informally recues yourself? Why did you not sign an official recusal or get an ethical review from the Treasury Department and/or the Office of Government Ethics?**

   Please see the answer to Question 1 above.

3. **You also stated at the hearing that while you recused yourself from the activities dealing with the negotiations over AIG's counterparty payments, you did leave your Chief of Staff in charge to deal with AIG. Is that correct? If not, did your Chief of Staff have any knowledge of the AIG counterparty payments?**

   That is not correct. In accordance with established practice, my colleagues and staff, led by First Vice President Christine Cumming, carried out the day-to-day management operations of the Federal Reserve Bank of New York. Ms. Cumming is the second ranking officer in the Bank, and also serves as its chief operating officer. Management and staff at the Bank also worked in close cooperation with their colleagues at the Federal Reserve Board.

4. **Is your current Chief of Staff a former employee of Goldman Sachs?**

   My chief of staff Mark Patterson worked at Goldman Sachs for approximately four years. He resigned over two years ago. Mr. Patterson has spent the bulk of his career in public service as a U.S. Senate staff member. From 1999 to 2004, he served as Policy Director for Senate Democratic Leader Tom Daschle. Before that he was for more than 10 years an aide to the late Senator Daniel Patrick Moynihan of New York, serving from 1995 to 1999 as Democratic Staff Director and Chief Counsel of the Senate Finance Committee, and from 1993 to 1995 as Senator Moynihan's Legislative Director.

Upon joining Treasury, Mr. Patterson signed the Obama Administration's Ethics Pledge, which is the strictest ever adopted by any Administration.

I trust that Mr. Patterson has complied fully with all of his ethical obligations. Any suggestion that Mr. Patterson would in his work at Treasury represent any interest other than the public interest is false and deeply unfair to him. He is a man of exceptional integrity, and he has a deep and sincere commitment to public service.

5. **Was your former Chief of Staff, while you were President of the FRBNY, a former employee of Goldman Sachs?**

   No. My chief of staff at the Federal Reserve Bank of New York never worked for Goldman Sachs. He is a former officer in the United States Navy.

6. **How can you assure American taxpayers that your Chiefs of Staff always acted in the best interest of the taxpayers and not of Goldman Sachs? What assurances can you give us?**

   These are people of the highest integrity working to serve the public interest. They have operated under exceptional circumstances with no precedent. Please also see the answer to Question 4 above.

7. **Do you believe that without the counterparty payments being made to AIG – at par value – that AIG would have been pushed into bankruptcy and a revolution would have resulted in this country? You inferred this during your testimony, but please clarify this for the record.**

   As I discussed in detail in my testimony before the Committee, the crisis that unfolded was so severe, damaging the lives of so many Americans, that it is hard for people to imagine how things could have been dramatically worse if AIG had been allowed to default. But I am confident that had we not acted, the crisis would have caused even more devastation, more hurt, and would have cost far more money.

Rep. Roy Blunt, Participating by Unanimous Consent of the Committee

1. **We now know that several of AIG's counterparties were experiencing significant financial difficulties at the time of the decision to purchase the counterparty contracts. How much was the health of these banks a factor in paying them 100 cents on the dollar for the value of their credit default swap contracts?**

   The financial health of individual counterparties was not a consideration. All of the counterparties were treated the same.

2. **Did the Federal Reserve Bank of New York's decision to treat all counterparties equally give the major counterparties (including foreign banks) effective veto power over the possibility of a concession from any other major parties?**

   Due to the nature of the contracts that AIG had entered into when selling insurance on the troubled securities, the contractual rights of the counterparties were very well protected. The counterparties had purchased insurance from AIG that entitled them, as a matter of law, to the full or par value of the contracts.

   In addition, the contracts between AIG and the counterparties afforded the counterparties the right to payments of cash collateral under certain circumstances. As a consequence, the value of the securities that the counterparties held, combined with the collateral that they had already obtained from AIG was generally equal to the par value of the securities. If AIG had defaulted, or even filed for bankruptcy, the counterparties would have kept both the collateral and the underlying securities.

   For additional information about the negotiations, I would refer you to the testimony before the Committee by Thomas Baxter, General Counsel of the Federal Reserve Bank of New York.[32]

3. **What was the extent of the negotiations over paying the counterparties at par value, and what will these same parties do in future times of crisis if Congress enacts legislation to mandate the creation of a $200 billion bailout fund?**

   The answer to Question 2, above, discusses the negotiations with the AIG counterparties in 2008. The second part of your question addresses the comprehensive financial reform legislation that the President has proposed. There are two central lessons from this recent crisis, both applicable to AIG, that have guided the President's proposals and the legislation now working through Congress.

   First, the government needs the ability to limit risk-taking for institutions that threaten the overall stability of the system and can cause extraordinary damage to the American economy. The government needs this ability not just for banks, but for institutions that operate like banks. These non-bank financial institutions have existed alongside banks and yet were not

[32] Thomas C. Baxter Jr., *Factors Affecting Efforts to Limit Payments to AIG Counterparties*, Testimony before the Committee on Government Oversight and Reform, January 27, 2010.

subject to those constraints in this crisis. The government also needs to make sure that regulators have accountability and flexibility, and that they enforce sensibly-designed constraints on risk.

Second, the government must have the ability to resolve failing major financial institutions in an orderly manner, with losses absorbed not by taxpayers but by equity holders, unsecured creditors and, if necessary, other large financial institutions. This resolution authority would allow an orderly response to a potential future crisis, protecting both the taxpayer and the overall economy.

4. **What was the rationale for keeping secret the list of par value counterparties, given that the SIGTARP concludes that "there is no indication that AIG's disclosure undermined the stability of AIG or the market or damage legitimate interests of the counterparties"?**

   In March 2009, in response to requests by Congress that the identities of the counterparties be made public, I understand that AIG decided to disclose the counterparty names. I was not involved in this decision. However, the circumstances in March 2009 were very different than those in 2008. By March 2009, government assistance had succeeded in stabilizing AIG, and Maiden Lane III had completed the purchase of the securities from the counterparties. In addition, AIG had decided to wind down its AIG Financial Products derivatives business.

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

DENNIS BLACK, *et al.*, Plaintiffs, v. PENSION BENEFIT GUARANTY CORPORATION, *et al.*, Defendants.	No. 2:09-cv-13616-AJT-DAS MOTION OF DEFENDANTS U.S. DEPARTMENT OF THE TREASURY, PRESIDENTIAL TASK FORCE ON THE AUTO INDUSTRY, TIMOTHY F. GEITHNER, STEVEN L. RATTNER, AND RON A. BLOOM TO DISMISS OR, IN THE ALTERNATIVE, FOR SUMMARY JUDGMENT

Defendants U.S. Department of the Treasury, Presidential Task Force on the Auto Industry, Timothy F. Geithner, Steven L. Rattner, and Ron A. Bloom (Treasury Defendants) hereby move pursuant to Fed. R. Civ. 12(b)(1) and 12(b)(6) to dismiss this action for lack of subject matter jurisdiction and for failure to state a claim upon which relief can be granted. In the alternative, Treasury Defendants move pursuant to Fed. R. Civ. P. 56(b) for summary judgment. The grounds for Treasury Defendants' motion are set forth in the memorandum submitted herewith.

Counsel for plaintiff advises that he opposes the relief that Treasury Defendants hereby seek.

In view of the filing of this motion, Treasury Defendants hereby withdraw their pending motion for extension of time (Dkt. 105).

Respectfully submitted,

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Dated: February 16, 2010

CERTIFICATE OF SERVICE

I hereby certify that on February 16, 2010, I served the motion of defendants U.S. Department of the Treasury, Presidential Task Force on the Auto Industry, Timothy F. Geithner, Steven L. Rattner, and Ron A. Bloom to dismiss or in the alternative, for summary judgment, the memorandum in support of that motion, the exhibits to the motion, except Exs. D and M, and the proposed order by ordinary mail or electronically.

s/ *David M. Glass*

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

	)	No. 2:09-cv-13616-AJT-DAS
DENNIS BLACK, *et al.*,	)	
	)	MEMORANDUM IN SUPPORT OF THE
Plaintiffs,	)	MOTION OF DEFENDANTS U.S.
	)	DEPARTMENT OF THE TREASURY,
v.	)	PRESIDENTIAL TASK FORCE ON THE
	)	AUTO INDUSTRY, TIMOTHY F.
PENSION BENEFIT GUARANTY	)	GEITHNER, STEVEN L. RATTNER, AND
CORP., *et al.*,	)	RON A. BLOOM TO DISMISS OR, IN
	)	THE ALTERNATIVE, FOR SUMMARY
Defendants.	)	JUDGMENT
	)	

STATEMENT OF ISSUES PRESENTED

1. Do plaintiffs have standing to sue defendants U.S. Department of the Treasury, Presidential Task Force on the Auto Industry, Timothy F. Geithner, Steven L. Rattner, or Ron A. Bloom (Treasury Defendants) over the agreement of defendant General Motors LLC (New GM) to make supplemental payments to certain retirees of Delphi Corp. (Delphi) represented by the United Auto Workers (UAW), United Steel Workers (USW), or International Union of Electronic Workers (IUE)?

2. Did New GM act as a government instrumentality when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE?

3. Did New GM deny plaintiffs equal protection, freedom of association, or freedom of speech when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE even assuming, *arguendo*, that it acted as a government instrumentality when it agreed to make those payments?

4. Are plaintiffs entitled to an order directing Treasury Defendants to provide further loan assistance to New GM or to an award of damages against defendants Geithner, Rattner, or Bloom even assuming, *arguendo*, that they are entitled to other forms of relief?

CONTROLLING OR MOST APPROPRIATE AUTHORITY
FOR RELIEF SOUGHT

Albright v. Longview Police Dep't, 884 F.2d 835 (5th Cir. 1989)

Am. Mfrs. Mut. Ins. Co. v. Sullivan, 526 U.S. 40 (1999)

Ashcroft v. Iqbal, 129 S. Ct. 1937 (2009)

Brentwood Acad. v. Tenn. Secondary Sch. Ath. Ass'n, 531 U.S. 288 (2001)

Campbell v. PMI Food Equip. Group, 509 F.3d 776 (6th Cir. 2007)

Cent. States, S.E. & S.W. Areas Pension Fund v. Reimer Express World Corp., 230 F.3d 934 (7th Cir. 2000)

Club Italia Soccer & Sports Org. v. Twp. of Shelby, 430 F.3d 286 (6th Cir. 2006)

Day v. Bond, 500 F.3d 1127 (10th Cir. 2007)

Henry v. Metro Sewer Dist., 922 F.2d 332 (6th Cir. 1990)

Hoke Co. v. TVA, 854 F.2d 820 (6th Cir. 1988)

Hook v. United States, 2008 WL 4424811 (D. Colo. Sept. 25, 2008)

Hoopa Valley Tribe v. United States, 86 Fed. Cl. 430 (2009)

In re Gen. Motors Corp., 407 B.R. 463 (Bankr. S.D.N.Y. 2009)

Lujan v. Def. of Wildlife, 504 U.S. 555 (1992)

Lyng v. UAW, 485 U.S. 358 (1988)

Memphis Am. Fed. Teachers v. Bd. of Educ., 534 F.2d 699 (6th Cir. 1976)

OPM v. Richmond, 496 U.S. 414 (1990)

San Fran. Arts. & Ath., Inc. v. U.S. Olympic Comm., 483 U.S. 522 (1987)

Spagnola v. Mathis, 859 F.2d 223 (D.C. Cir. 1988)

Vistein v. Am. Registry of Radiological Tech., 342 F. App'x 113 (6th Cir. 2009)

Wilson v. Layne, 526 U.S. 603 (1999)

Wolotsky v. Huhn, 960 F.2d 1331 (6th Cir. 1992)

TABLE OF EXHIBITS

Ex. P.	*In re Delphi Corp.*, No. 05-44481 (RDD) (Bankr. S.D.N.Y.), Not. Filing of Settlement Agreement Betw. Delphi Corp. and the Pension Benefit Guarantee Corp. (July 21, 2009)
Ex. Q.	DPH Holdings Corp., Notice (Undated)
Ex. R.	Settlement Agreement Between and Among GMCo/MLC - IUE-CWA and USW Regarding Retiree Health Care, Life Insurance, Pension Top-Up, and Modification and GMCo Assumption of MLC - IUE-CWA CBA (Sept. 10, 2009)
Ex. S.	William Ehart & Andrea Billups, *Nonunion Auto Retirees Cry Foul in Treasury Deal; Ex-Delphi Workers Cite Pension Inequity*, Wash. Times (Dec. 24, 2009)

PRELIMINARY STATEMENT

Plaintiffs are three salaried retirees of Delphi Corp. (Delphi) and the Delphi Salaried Retiree Association. Salaried retirees of Delphi are retirees who are not represented by a union. Suing the Pension Benefit Guarantee Corp. (PBGC); General Motors LLC (New GM)[1]; the U.S. Department of the Treasury (UST); the Presidential Task Force on the Auto Industry (Auto Task Force); three present or former officials of UST, Timothy F. Geithner, Steven L. Rattner, and Ron A. Bloom; and certain agents, employees, or representatives of UST or the Auto Task Force whose identity is unknown to plaintiffs (DOES 1-50), plaintiffs allege that PBGC acted unlawfully by entering into one or more agreements with Delphi terminating plaintiffs' pension plan. In addition, plaintiffs allege that New GM denied them equal protection, freedom of association, and freedom of speech by agreeing to make supplemental payments to certain retirees of Delphi represented by the United Auto Workers (UAW), United Steel Workers (USW), or International Union of Electronic Workers (IUE)[2] but not agreeing to make supplemental payments to plaintiffs.

To remedy the alleged denial of equal protection, freedom of association, and freedom of speech, plaintiffs seek both "specific relief" and damages. The "specific relief" that plaintiffs seek is an order directing UST, the Auto Task Force, and defendants Geithner, Rattner, Bloom, and DOES 1-50 to direct New GM to take certain actions "to afford the salaried retirees [of Delphi] the same benefits afforded to the union-affiliated retirees * * *, providing additional loan

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[1] Until October 19, 2009, New GM was known as General Motors Co. Gen. Motors Co., Rep. on Form 8-K (Oct. 19, 2009), Item 8.01.

[2] Effective October 1, 2000, IUE merged with the Communications Workers of America (CWA) to become the Industrial Division of CWA (IUE-CWA). *See* Thomas J. Sheeran, *Gore Applauds Merger of Unions*, Akron Beacon Journal (Sept. 24, 2000) at C7. "IUE" is used in this memorandum to refer to IUE prior to the merger and to IUE-CWA following the merger.

assistance to New GM if necessary"; and directing New GM to take such actions as UST, the Auto Task Force, or defendants Geithner, Rattner, Bloom, or DOES 1-50 direct it to take. The damages that plaintiffs seek consist of an award of damages against New GM and against defendants Geithner, Rattner, Bloom, and DOES 1-50 under *Bivens v. Six Unknown Named Agents of the Federal Bureau of Narcotics*, 403 U.S. 388 (1971), "for [allegedly] denying Plaintiffs the same benefits provided to the similarly situated union-affiliated retirees on the basis of their non-union affiliation, in violation of their rights to equal protection."

As is shown below, plaintiffs do not have standing to sue UST, the Auto Task Force, or defendants Geithner, Rattner, or Bloom (Treasury Defendants). Even assuming, *arguendo*, that plaintiffs have standing to sue Treasury Defendants, no denial of equal protection, freedom of association, or freedom of speech has taken place here, both because New GM has not acted as a government instrumentality and even assuming, *arguendo*, that it has. Even assuming, *arguendo*, that any denial of equal protection, freedom of association, or freedom of speech has taken place here, plaintiffs are not entitled to an order directing Treasury Defendants to provide further loan assistance to New GM or to an award of damages against defendants Geithner, Rattner, or Bloom. For all of these reasons, this action should be dismissed as to Treasury Defendants.[3]

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[3] For the same reasons, this action should also be dismissed as to DOES 1-50. In addition, this action should be dismissed as to DOES 1-50 because "[c]ourts lack personal jurisdiction over unidentified fictitious defendants," *King v. Forest*, 2008 WL 4951049, at *4 (N.D. Tex. Nov. 14, 2008), and because "fictitious party pleading is [generally] not permitted in federal court." *Hester v. Lowndes County Comm'n*, 2006 WL 2547430, at *9 (M.D. Ala. Sept. 1, 2006).

STATEMENT OF FACTS

A. General Motors Corp. (Old GM) and Delphi

"Trac[ing] its roots back to 1908," Old GM was "primarily engaged in the world-wide production of cars, trucks and parts." *See In re Gen. Motors Corp.*, 407 B.R. 463, 475 (Bankr. S.D.N.Y. 2009); Ex. A at 1.[4] As of March 31, 2009, Old GM had a workforce in the United States of approximately 91,000, of whom approximately 62,000 were represented by unions. *Gen. Motors*, 407 B.R. at 475. Approximately 98% of the employees who were represented by unions were represented by UAW. *Id.* As of July 5, 2009, Old GM was "the largest Original Equipment Manufacturer ('OEM') in the U.S., and the second largest in the world." *Id.* (emphasis omitted).

Delphi began as the "Delphi Automotive Systems business sector of [Old] GM." *See* Ex. B, Ex. 99.1 at 1. "[O]n September 16, 1998, Delphi was incorporated as a wholly-owned subsidiary of [Old] GM." *Id.* "[E]ffective as of January 1, 1999, [Old] GM contributed to Delphi the assets, and Delphi assumed the liabilities, comprising the business of the Delphi Automotive Systems business sector of [Old] GM." *Id.* "[O]n Feburary 10, 1999, Delphi consummated an initial public offering of 100,000,000 shares of its common stock." *Id.* "[O]n May 28, 1999, [Old] GM distributed 542,565,000 shares of Delphi common stock as a dividend to holders of GM $1-2/3 par value common stock and contributed 13,435,000 shares of Delphi common stock to a trust for the benefit of [Old] GM employees, with the effect that [Old] GM divested its entire equity interest in Delphi on that date." *Id.*

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[4] References to exhibits are to the exhibits to this motion.

In connection with the spin off of Delphi from Old GM, separate pension plans for salaried and hourly employees of Delphi were spun off from the pension plans for salaried and hourly employees that Old GM maintained. *See* Ex. C at 5. Delphi was the sponsor and administrator of the spun-off plans. *Id.* At the time of the spin off, the Delphi pension plan for salaried employees was fully funded but the Delphi pension plan for hourly employees was not. *See* Ex. D at 162:8-15.[5]

At or about the time that Delphi was spun off from Old GM, Old GM entered into benefit guarantee agreements with UAW, USW, and IUE. *See* Ex. B at 3. Among other things, those agreements required Old GM to make "supplemental payments" to any "retired Covered Employee[]" who received pension benefits on or before October 18, 2007, "at a level below that called for in any applicable [Delphi/UAW, Delphi/USW, or Delphi/IUE] agreement or pension plan due to Financial Distress." *Id.*, Ex. 99.2 ¶ (e), Ex. 99.4 ¶ (e), Ex. 99.5 ¶ (e); *see id.* at 4. With certain exceptions, "Covered Employees" were defined in the benefit guarantee agreements as Delphi employees represented by UAW, USW, or IUE who had "unbroken seniority and were employed by [Old] GM under the terms of the [then-current national agreement between Old GM and UAW, USW, or IUE] as of the spin-off of Delphi from [Old] GM on May 28, 1999." *Id.*, Ex. 99.2 at 1, Ex. 99.4 at 1, Ex. 99.5 at 1. Accordingly, salaried employees of Delphi were not

[5] Ex. D is the transcript of the deposition of Matthew Feldman in *In re DPH Holdings Corp.*, No. 05-44481 (RDD) (Bankr. S.D.N.Y.). Ex. M is the transcript of the deposition of Harry Wilson in *In re Motors Liquidation Co.*, No. 09-50026 (REG) (Bankr. S.D.N.Y.). Exs. D and M are not being served or filed at this time because certain protective orders in *DPH Holdings* and *Motors Liquidation* may govern portions of those exhibits not quoted in this memorandum. To avoid violating those orders, Treasury Defendants have been trying to confirm that the parties to those orders have no objection to the service and filing of Ex. D or M in this action. Those efforts are continuing.

defined as "Covered Employees" for purposes of the benefit guarantee agreements. *See id.* The "supplemental payments" that Old GM was required to make to Covered Employees were payments equal to the pension benefits called for "in the [Delphi/UAW, Delphi/USW, or Delphi/IUE] agreement applicable at the time," minus "any pension benefits received (x) from a pension plan sponsored by Delphi, any of its subsidiaries or affiliates, or any of their successor compani(ies), (y) from the PBGC, and/or (z) from a pension plan sponsored by [Old] GM." *Id.*, Ex. 99.2 ¶ e(1), Ex. 99.4 ¶ e(1), Ex. 99.5 ¶ e(1).

On October 8, 2005, "Delphi and 38 of its domestic U.S. subsidiaries filed voluntary petitions for business reorganization under chapter 11 of the U.S. Bankruptcy Code." Ex. E at 1. At the time those petitions were filed, "Delphi expect[ed] to complete its U.S.-based restructuring and emerge from chapter 11 business reorganization in early to mid-2007." *Id.* at 1-2. However, the Delphi bankruptcy "remained mired in a morass" through the spring of 2009. *See* Ex. D at 37:14-15.

As late as 2009, Delphi supplied "more than 3,000 parts to [Old GM]." *See* Ex. D at 24:24-25. To try to keep Delphi afloat during the pendency of the Delphi bankruptcy, Old GM "invested and funded Delphi with literally billions of dollars ." *Id.* at 37:9-11.

B. The Financial Crisis in the U.S. Auto Industry

"[I]n the fall of 2008, the combination of rising gasoline prices, tightening credit markets, eroding consumer confidence, high unemployment, and discretionary spending concerns prompted a significant downturn in automobile sales in the United States and abroad." Ex. F at 7. By early December 2008, Old GM and Chrysler Holding LLC (Chrysler) "could no longer secure the credit they needed to conduct their day-to-day operations." *Id.* at 3. "Unless they could raise billions of dollars in new financing, they faced collapse – a potentially crippling blow to the American economy that [UST] estimated would eliminate nearly 1.1 million jobs." *Id.*

On December 4, 2008, the chief executive officers of Old GM and Chrysler "appeared before Congress and appealed for government assistance to help them stay afloat." Ex. F at 8 & nn.12-13. When Congress did not enact remedial legislation, the Administration announced that it would "consider making [Troubled Assets Relief Program (TARP)] funds available to the automotive industry."[6] *Id.* at 3, 8. "Under the Automobile Industry Financing Program (AIFP) that was announced on December 19, [2008], Chrysler and [Old] GM received bridge loans of $4 billion and $13.4 billion, respectively, under separate loan and security agreements." *Id.* at 8. "The [Old] GM loan and security agreement was signed on December 31, 2008 and * * * [t]he Chrysler loan and security agreement was signed on January 2, 2009." *Id.* at 8-9

"The AIFP loans were extended to Chrysler and [Old] GM under terms and conditions specified in the loan agreements." Ex. F at 9. "The most important condition required each company to demonstrate that the assistance would allow it to achieve 'financial viability,' which was defined as 'positive net value, taking into account all current and future costs, and [the ability to] fully repay the government loans.'" Id. "Both companies were required to submit viability plans designed 'to achieve and sustain [their] long-term viability, international competitiveness and energy efficiency.'" *Id.* "Key to such viability would be 'meaningful

[6] Legislation enacted on October 3, 2008, authorized the Secretary of the Treasury to "establish [TARP] to purchase, and to make and fund commitments to purchase, troubled assets from any financial institution, on such terms and conditions as are determined by the Secretary, and in accordance with this Act and the policies and procedures developed and published by the Secretary." Emergency Economic Stabilization Act of 2008 (EESA), Pub. L. No. 110-343, § 101(a)(1), 122 Stat. 3767 (2008) (codified at 12 U.S.C. § 5211(a)(1)).

concessions from all involved in the automotive industry.'" *Id.* "The loans also imposed conditions and covenants related to their operations, expenditures, and reporting thereof to the President's designee." *Id.*

C. The Auto Task Force

The Auto Task Force was established by the President on or about February 15, 2009, to "assume responsibility for reviewing the Chrysler and [Old] GM viability plans." *See* Ex. F at 10. Co-chaired by defendant Geithner, the Secretary of the Treasury, and by Larry Summers, Director of the National Economic Council (NEC), the Auto Task Force consists of 10 senior officials of the federal government. Ex. G at 1. Staffing for the Auto Task Force is provided by a team of UST and NEC personnel (Auto Team). *See* Ex. F at 10 n.31. Defendants Bloom and Rattner were named by the President to lead the Auto Team. *Id.* at 10-11. Defendant Bloom became the sole head of the Auto Team when defendant Rattner left the government to return to the private sector on or about July 13, 2009. *Id.* at 11; Ex. H.

In theory, the Auto Team reports to the Auto Task Force and its co-chairs, "who then report up to the President." *See* Ex. F at 10, 11. In practice, "[t]he missions and personnel" of the Auto Task Force and Auto Team "overlap considerably." *Id.* at 10 n.31. Accordingly, references to the Auto Task Force in this memorandum are to the Auto Task Force and Auto Team as a single entity.

D. The Restructuring Plans Submitted by Chrysler and Old GM; the Rejection of Those Plans; the Revised Restructuring Plan for Old GM; and the Acceptance and Implementation of That Plan

On February 17, 2009, Chrysler and Old GM submitted "detailed business plan[s] to [UST]." *See* Ex. I at 2, 3. On March 30, 2009, the President announced that the Auto Task

Force had completed its evaluation of the "requests by General Motors and Chrysler for additional government assistance, as well as [the] plans developed by each of these companies to restructure, to modernize, and to make themselves more competitive," but said that neither plan went "far enough to warrant the substantial new investment that these companies are requesting." Ex. J at 1. Stating that "[w]e cannot, and must not, and we will not let our auto industry simply vanish," the President announced that "[his] administration [would] offer [Old] GM and Chrysler a limited additional period of time to work with creditors, unions, and other stakeholders to fundamentally restructure in a way that would justify an investment of additional taxpayer dollars" but that both companies would need to "produce plans" during that period that would "give the American people confidence in their long-term prospects for success." *Id.*

Believing that the "long-term viability [of Old GM and Chrysler] and [their] ability to repay the taxpayer dollars they were receiving would be seriously undermined if the government became involved in day-to-day business decisions," the President "directed his Auto Task Force to take a commercial approach and refrain from intervening in the day-to-day decisions of these companies." Ex. I at 1. Accordingly, the President said the following when he announced that "[his] team [would] be working closely with [Old] GM [over the next 60 days] to produce a better business plan":

> Let me be clear. The United States government has no interest in running GM. We have no intention of running GM . What we are interested in is giving GM an opportunity to finally make those much needed changes that will let them emerge from this crisis a stronger and more competitive company.

Ex. J at 2.

During the 60 days that followed the President's announcement, "Treasury loaned an additional $6 billion to fund [Old] GM." *See* Ex. K at 3. In addition, Old GM "work[ed] with [its] stakeholders and the President's Auto Task Force" to "develop[] a more robust operating plan." *See* Ex. I at 1. During this time, the Auto Task Force spoke to "dozens of experts, advisors, consultants, industry experts, who collectively had thousands of years of experience in the automotive industry, as well as, obviously, the management team at great length." Ex. L at 182:19-183:11. The Auto Task Force concluded on the basis of these discussions that the only way to "achieve[] the company's primary goals and [UST's] primary goals of having a viable GM" was for Old GM to file a petition for reorganization under Chapter 11 of the Bankruptcy Code and to move for an order under §363 of the Bankruptcy Code, 11 U.S.C. § 363, permitting the assets of Old GM to be sold to a "Treasury-sponsored entity," New GM. *See id.* at 192:16-17; Ex. M at 14:1-15:21.[7] The Auto Task Force considered a sale under § 363 to be preferable to the development and implementation of a plan of reorganization under Chapter 11 because a sale under § 363 offered the possibility of "speed, certainty and the ability to leave behind liabilities that a commercial buyer would not want to have in the new company." Ex. M at 120:18-25.

"Once the decision was made to pursue a Section 363 sale," the Auto Task Force began to negotiate the details of the sale with Old GM, UAW, the UAW VEBA Trust,[8] certain of Old GM's unsecured lenders, and "anybody who approached us." *See* Ex. M at 15:16-22, 100:3-19,

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[7] *See* n. 5, *supra*.

[8] Old GM had used "trusts qualified as 'voluntary employee beneficiary associations' under the Internal Revenue Code [VEBAs] * * * to hold reserves to meet [Old] GM's future obligations to provide healthcare and life insurance benefits * * * to its salaried and hourly employees upon retirement." *Gen. Motors*, 407 B.R. at 478 n.7. "In substance, [an] employer makes contributions to [a] VEBA, and the VEBA funds the health benefits to the retirees." *Id.*

209:10. During these negotiations, the Auto Task Force "took dozens of meetings of various constituencies ranging from dealers to splinter unions to a whole host of different * * * parties in interest." *See* Ex. L at 81:6-9. In conducting these negotiations, the Auto Task Force possessed a "considerable" amount of "negotiating leverage" because the government was "the only buyer for these assets"; because "the only alternative" to the sale of the assets under § 363 "was a liquidation of [Old GM]"; and because the liquidation of Old GM would have been "worse for all concerned." Ex. M at 98:19-100:2, 103:18-12. Despite the negotiating leverage that the Auto Task Force possessed, the negotiations that the Auto Task Force conducted during this period were "intense [and] arms'-length." *Gen. Motors*, 407 B.R. at 494. Because the Auto Task Force considered itself to be negotiating "[f]or New GM," not "for Old GM," the negotiations between the Auto Task Force and Old GM were "[c]ontentious, often difficult, sometimes exasperating." *See id.* Ex. M at 15:23-16:5, 87:2-88:6; Ex. L at 181:3-8.

Negotiating the details of the proposed sale required the Auto Task Force to deal with "thousands of issues" in an "extraordinarily short period of time." *See* Ex. M at 295:13-16. Viewing itself as having "a fiduciary duty to use taxpayer dollars in the most appropriate way," the Auto Task Force sought to limit the expenditure of public funds to the minimum necessary to "get the deal done." *See id.* at 123:6-7, 361:20-24; Ex. L at 183:21-22. Accordingly, the standard that the Auto Task Force applied in evaluating particular aspects of the proposed sale was whether a particular action was "commercially necessary," "commercially reasonable," or "commercially the right thing to do," i.e., something that "a commercial buyer would do in this instance." *See* Ex. M at 17:9-19, 32:8-15, 39:19-40:4. 40:19-41:2, 46:17-24, 52:13-18, 123:4-5, 156:21-157:2, 291:8-16; 292:15-18, 311:9-11; Ex. L at 111:11-15.

In view of the foregoing, the question that the Auto Task Force asked whenever anyone suggested that a particular liability of Old GM be assumed by New GM was "what's the commercial basis, the commercial need for that liability to be brought to [New GM], why would a buyer buy that liability if he or she didn't have to." Ex. M at 88:18-25. The Auto Task Force answered this question by seeking to bring over to New GM only those liabilities of Old GM that it "thought were commercially necessary," i.e., necessary "in order for [New GM] to operate," and by seeking to "[leave] behind at Old GM" all other liabilities of Old GM. *See id.* at 263:20-23, 276:22-277:8, 291:10-16, 294:2-10, 302:16-19; Ex. L at 102:25-103:2, 111:23-25, 135:16-22. Accordingly, the Auto Task Force was forced to overlook whether a particular person or group would be harmed, even "tragic[ally]," if a particular liability were not brought over to New GM. *See* Ex. L at 126:4-9. In conducting its operations, the Auto Task Force did not attempt to use "[New] GM or Chrysler as an instrument of broader government policy" because doing so would have been "inconsistent" with its goal of "promoting strong and viable companies, which [could] be profitable and contribute to economic growth and jobs without Government support as quickly as possible." *See* Ex. I at 6.

By June 1, 2009, the negotiations among Old GM, other interested parties, and the Auto Task Force had produced a plan under which New GM would acquire "the bulk of [the] assets" of Old GM and assume "some, but only some, of [Old GM's] liabilities." *See Gen. Motors*, at 473, 496 (emphasis omitted). The liabilities that New GM would assume would include "all employment-related obligations and liabilities [of Old GM] under any assumed employee benefit plan relating to employees that are or were covered by the UAW collective bargaining agreement" but would not include any "employment-related obligations not otherwise assumed, including, among other obligations, those arising out of the employment, potential employment, or termination of any individual (other than an employee covered by the UAW collective bargaining agreement) prior to or at the closing." *Id.* at 482. "[M]ost of [UST's] loans to the Old GM" would be converted into 60.8% of the common stock of New GM and other securities. *See* Ex. K at 3. The other owners of the common stock of New GM would be the Government of Canada (11.7%); a new VEBA Trust (17.5%); and Old GM for the benefit of its unsecured creditors (10%). *See Gen. Motors*, 407 B.R. at 482-83; Ex. L at 128:21-25; Ex. N. The federal government would commit "approximately $30.1 billion of additional federal assistance from [TARP]," thus becoming "GM's largest pre- and post-petition creditor." Ex. I at 3; *Gen. Motors*, 407 B.R. at 473.

On June 1, 2009, Old GM "filed its chapter 11 petition" and moved for approval of the proposed sale under § 363. *Gen. Motors*, 407 B.R. at 473, 479; Ex. M at 78:25-79:6. On the same day, the President announced that "GM and its stakeholders," "[w]orking with [the]Auto Task Force," "ha[d] produced a viable, achievable plan that will give this iconic American company a chance to rise again." Ex. O at 2. Reiterating that "[w]hat we are doing – what I have no interest in doing – is running GM," the President said:

> GM will be run by a private board of directors and management team with a track record in American manufacturing that reflects a commitment to innovation and quality. They – and not the government – will call the shots and make the decisions about how to turn this company around. The federal government will refrain from exercising its rights as a shareholder in all but the most fundamental corporate decisions. When a difficult decision has to be made on matters like where to open a new plant or what type of new car to make, the new GM, not the United States government, will make that decision.

Id.

USW, IUE, and the International Union of Operating Engineers (IUOE) objected to the proposed sale on the ground that New GM would be assuming liability for medical and life insurance benefits owed by Old GM to retirees of Old GM represented by UAW but not for medical and life insurance benefits owed by Old GM to retirees of Old GM represented by USW, IUE, or IUOE. Overruling that objection, the court acknowledged that "UAW retirees [would] get a better result, after is said and done, than [USW, IUE, or IUOE retirees]." *Gen. Motors*, 407 B.R. at 512. However, the court held that the disparity in treatment did not result from "a conscious decision" that "retirees [of USW, IUE, and IUOE] would not be offered as good a deal as others" and said:

> [A]s a matter of reality, [New GM] needs a properly motivated workforce to enable [it] to succeed, requiring it to enter into satisfactory agreements with the UAW – which includes arrangements satisfactory to the UAW for UAW retirees. And [New GM] is not similarly motivated, in triaging its expenditures, to assume obligations for retirees of unions whose members, with little in the way of exception, no longer work for GM.
>
> * * * * [UST], in making hard decisions about where to spend its money and make New GM as viable as possible, made business decisions that it was entitled to make, and the fact that there were so few [employees represented by USW, IUE, or IUOE] still working for GM was an understandable factor in that decision.

Id.

Accordingly, the court approved the proposed sale under § 363 by decision dated July 5, 2009. *Gen. Motors*, 407 B.R. at 520. The sale was completed on July 10, 2009. *See* Ex. I at 3. By statement dated July 13, 2009, defendant Geithner announced that "the government [would be] transitioning its role away from restructuring to monitoring this vital industry and protecting the substantial investment the American taxpayers have made in GM, Chrysler, and GMAC."

Ex. H. On July 27, 2009, defendant Bloom told the Congressional Oversight Panel[9] that, "[a]s a common shareholder [in New Chrysler and New GM], the government [would] only vote on core governance issues, including the selection of a company's board of directors and major corporate events or transactions," and that, "[w]hile protecting taxpayer resources, the government intend[ed] to be extremely disciplined as to how it intend[ed] to use even those limited rights." Ex. I at 7 (emphasis omitted).

E. The Agreement of New GM to Make Supplemental Payments to Certain Retirees of Delphi Represented by UAW

The subject of "the Delphi pensions" was "probably first raised" in a conversation between PBGC and the Auto Task Force "in maybe April of 2009." Ex. D at 156:10-18. However, the Auto Task Force did not raise the subject with Old GM "until, you know, the middle of May or even the last half of May of 2009." *Id.* at 156:19-22. The role that the Auto Task Force sought to play with respect to those pensions was to "act[] as sort of facilitator and intermediary between the PBGC and General Motors." Ex. D at 155:20-25. The outcome that the Auto Task Force anticipated with respect to the pensions was "an agreement where the [Delphi] salaried plan would get terminated and taken over by the PBGC and General Motors would assume liability for the [Delphi] hourly plans." *Id.* at 159:10-160:2. As the Auto Task Force has explained:

> We thought there was a reasonable argument for General Motors, particularly on the UAW side, that since most of the likely outcomes would have some of the UAW plans coming back to General Motors that it would be problematic for General Motors to sort of push the termination of the hourly plan related to the UAW. * * * *

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[9] Established by EESA, the Congressional Oversight Panel is "an establishment in the legislative branch" that "review[s] the current state of the financial markets and the regulatory system and submit[s] [certain] reports to Congress." EESA §§ 125(a), (b), 122 Stat. 3791.

> When the plans got transferred to Delphi in '99, the [salaried] plan was a fully funded plan at that point. We didn't think it made sense for General Motors to take that plan back under its umbrella. And the hourly plans were not fully funded at that time, so we thought it was a little bit after different circumstance.

Id. at 161:15-162:15.

On or about June 3, 2009, Old GM advised the Auto Task Force that

> they had assumed [the Delphi hourly plan] would get terminated but that they would honor the top-up guarantee with respect to the UAW, and that that that was something that, in their bargaining with the UAW around the General Motors bankruptcy and the new UAW agreement, that they had agreed to bring that across to new General Motors and they were prepared to honor that obligation.

See Ex. D at 168:21-25, 176:3-12.

However, Old GM further advised the Auto Task Force that New GM did not intend to assume liability for the Delphi hourly plan as a whole because "[it] had not built into [its] business plan sufficient funding to take on [that plan], and [it was] concerned about the impact of that on [its] own reorganization." *See* Ex. D at 169:5-14. After conducting its own analysis, the Auto Task Force reached the same conclusion, i.e., that the Delphi hourly plan "was a 3 billion-dollar liability that [New GM] could not afford." *Id.* at 183:5-184:15.

F. The Resolution of the Delphi Bankruptcy and the Agreement of New GM to Make Supplemental Payments to Certain Retirees of Delphi Represented by USW or IUE

On June 16, 2009, Delphi filed a modified plan of reorganization in its bankruptcy proceedings. Ex. P at 1-2. As approved by the court on July 30, 2009, the modified plan called for "the acquisition of substantially all of [the] global core businesses [of Delphi] by a group of private investors" and the acquisition of Delphi's "non-core steering business and certain US manufacturing plants" by an affiliate of New GM. *See In re Delphi*, 2009 WL 2482146, at *37

(Bankr. S.D.N.Y. July 30, 2009); Ex. Q at 1. The modified plan was "substantially consummated" on October 6, 2009. Ex. Q at 1.

By agreement dated July 21, 2009, Delphi authorized PBGC to seek a court order permitting the Delphi hourly plan to be terminated. Ex. P, Ex. 1 ¶ 3(b). By the same agreement, Delphi agreed to execute agreements with PGBC terminating the other Delphi pension plans, including the pension plan for salaried retirees, and placing those plans under the trusteeship of PBGC for the purpose of the payment of benefits. *Id.*, Ex. 1 ¶¶ 3(a), (b)(i). Referencing the agreement between Delphi and PBGC, New GM issued a statement on July 21, 2009, addressing its "responsibility toward Delphi's pension plans, given that many of those covered were [Old GM] employees prior to [Old GM's] spinning off Delphi in 1999." Ex. A at 1. Stating that Old GM had made "appropriate provisions for the plans at the time of the spin-off," that Delphi had become "responsible for the plans from that point forward," and that Old GM had agreed "[a]s a result of bargaining at the time of the spin-off * * * to top-up pension benefits for certain limited groups of employees and retirees in the event that the Delphi hourly pension plan was terminated," New GM announced that it would "honor these commitments," just as it was honoring "other union agreements that it ha[d] assumed from the old GM." *Id.*

At or about this time, USW and IUE "assert[ed]" that "[New GM] and/or [Old GM]" were required to "continue to provide retiree medical benefits in accordance with [certain] collective bargaining agreements and [a certain] class settlement agreement" and further asserted that "[New GM] and/or [Old GM]" were required to "provide certain pension benefit guarantees in accordance with collectively bargained memorandums of understanding regarding establishment or restructuring of Delphi." *See* Ex. R at 1. New GM and Old GM "den[ied]" those "assert[ions]." *Id.*

By agreement with USW and IUE dated September 10, 2009, Old GM and New GM agreed to "resolve all claims regarding such matters," "[a]fter due consideration of the factual and legal arguments regarding these issues, as well as the costs, risks, and delays associated with litigating [them]." Ex. R at 1. Under the heading of "Pension Top-Up," the agreement provided that New GM would make supplemental payments to retirees of Delphi represented by USW or IUE in accordance with the benefit guarantee agreements into which Old GM had entered with USW and IUE at the time of the Delphi spin off in 1999. *See id.* ¶ 1. However, the agreement further provided that no retiree of Delphi represented by the International Association of Machinists, International Brotherhood of Electrical Workers, certain locals of the Michigan Regional Council of Carpenters, International Brotherhood of Teamsters, International Brotherhood of Boilermakers, IUOE, or United Catering Workers would be "eligible for the Pension Top-Up regardless of their election to participate in [certain] retiree health care and life insurance coverages contemplated by [this agreement]." *Id.* ¶¶ (1)(a), 5(a).

ARGUMENT

I. PLAINTIFFS DO NOT HAVE STANDING TO SUE TREASURY DEFENDANTS.

"Constitutional standing requires a plaintiff to 'allege personal injury fairly traceable to the defendant's allegedly unlawful conduct and likely to be redressed by the requested relief.'" *Club Italia Soccer & Sports Org. v. Charter Twp. of Shelby*, 470 F.3d 286, 291 (6th Cir. 2006) (quoting *Allen v. Wright*, 468 U.S. 737, 751 (1984)). The plaintiff "bears the burden of demonstrating standing and must plead its components with specificity." *Campbell v. PMI Food Equip. Group*, 509 F.3d 776, 783 (6th Cir. 2007).

"[W]hen the plaintiff is not himself the object of the government action or inaction he challenges, standing is not precluded, but it is ordinarily 'substantially more difficult' to establish." *Lujan v. Def. of Wildlife*, 504 U.S. 555, 562 (1992) (quoting *Allen*, 468 U.S. at 758). Accordingly, a plaintiff who wishes to contest another person's receipt of a benefit must allege that he or she has been injured by the other person's receipt of that benefit and must further allege that he or she would have been entitled to the benefit even if the other person had not received it. *See, e.g., Hoopa Valley Tribe v. United States*, 86 Fed. Cl. 430 (2009); *Day v. Bond*, 500 F.3d 1127 (10th Cir. 2007). In *Hoopa Valley*, an Indian tribe and its members were held to lack standing to challenge the government's "distribution to [another tribe] of certain monies from a trust fund created by [a particular statute]" because "[the] Plaintiffs already ha[d] received the amount of the Fund to which they [were] entitled, and could not be injured by distribution of monies to which they ha[d] no right." 86 Fed. Cl. at 436. In *Day*, individuals who were required to pay out-of-state tuition to attend state universities in Kansas were held to lack standing to challenge a Kansas statute permitting "certain illegal aliens to qualify for in-state tuition rates" because:

(1) the record contained no evidence of "any causal relationship between the tuition cost imposed on Kansas' public universities by [the statute] and nonresident tuition rates imposed on the Plaintiffs";

(2) the record contained no evidence that "Kansas public universities' budgets [were] a zero-sum game or that the higher nonresident tuition rates that illegal aliens would pay in the absence of [the statute] would even be available for redistribution [through] tuition reductions or educational services benefitting nonresident students like the Plaintiffs"; and

(3) none of the plaintiffs would "be eligible to pay resident tuition under [the statute] even if the allegedly discriminatory test of [the statute] favoring illegal aliens were stricken" because none of the plaintiffs "attended Kansas high schools for at least three years and either graduated from a Kansas high school or received a Kansas GED certificate."

500 F.3d at 1130, 1133-35, 1139.

In this case, plaintiffs do not allege that they have lost any benefits as a result of the agreement of New GM to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE. Neither do plaintiffs allege that they have suffered any other "'personal injury fairly traceable to [that agreement],'" much less any injury "'likely to be redressed by the requested relief.'" *See Club Italia*, 470 F.3d at 291 (quoting *Allen*, 468 U.S. at 758). To the contrary, the sole allegation that plaintiffs make with respect to the agreement is that it "has benefited union-affiliated retirees." 1st Am. Compl. ¶ 59. That allegation is not an allegation of injury. As plaintiff Dennis Black has said: "We don't begrudge the union retirees. We're happy they have remained whole; they earned it." Ex. S at 2.

Because plaintiffs do not allege that they have been injured by the agreement, they do not have standing to challenge it. *See Club Italia*, 470 F.3d at 291. Much less do they have standing to challenge the role that anyone may have played in bringing it into existence. As to Treasury Defendants, this action should therefore be dismissed.

II. NO DENIAL OF EQUAL PROTECTION, FREEDOM OF ASSOCIATION, OR FREEDOM OF SPEECH HAS TAKEN PLACE HERE BECAUSE NEW GM HAS NOT ACTED AS A GOVERNMENT INSTRUMENTALITY.

"[A] private actor [cannot] actionably suppress first amendment rights nor violate the due process clause." *Albright v. Longview Police Dep't*, 884 F.2d 835, 841 (5th Cir. 1989). Accordingly, private entities "will not be held to constitutional standards unless 'there is a sufficiently close nexus between the State and the challenged action of the regulated entity so that the action of the latter may be fairly treated as that of the State itself.'" *Am. Mfrs. Mut. Ins. Co. v. Sullivan*, 526 U.S. 40, 52 (1999) (quoting *Jackson v. Metro. Edison Co.*, 419 U.S. 345, 350 (1974)). "The Supreme Court has established four tests for determining whether the challenged conduct may be fairly attributable to the State." *Vistein v. Am. Registry of Radiological Tech.*, 342 F. App'x 113, 127 (6th Cir. 2009). "Those tests are (1) the public function test; (2) the state compulsion test; (3) the symbiotic relationship or nexus test; and (4) the entwinement test." *Id.*

In this case, plaintiffs allege that New GM acted as a government instrumentality under the entwinement test and the state compulsion test when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE. *See* 1st Am. Compl. ¶ 62. As is shown below, however, New GM did not act as a government instrumentality under either test.

A. New GM Did Not Act as a Government Instrumentality Under the Entwinement Test When It Agreed to Make Supplemental Payments to Certain Retirees of Delphi Represented by UAW, USW, or IUE.

"The entwinement test requires that the private entity be 'entwined with governmental policies' or that the government be 'entwined in [the private entity's] management or control.'" *Vistein*, 342 Fed. App'x at 128 (quoting *Brentwood Acad. v. Tenn. Secondary Sch. Ath. Ass'n*, 531 U.S. 288, 298 (2001)). The "crucial inquiry under the entwinement test is whether the 'nominally private character' of the private entity 'is overborne by the pervasive entwinement of public institutions and public officials in its composition and workings [such that] there is no substantial reason to claim unfairness in applying constitutional standards to it.'" *Id.* (quoting *Brentwood*, 531 U.S. at 298).

In this case, plaintiffs allege that New GM acted as a government instrumentality under the entwinement test when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE because "the U.S. Government * * * was GM's largest pre- and post-petition creditor" and because UST became the owner of 60.8% of New GM's common stock in connection with the sale of Old GM's assets under § 363. *See* 1st Am. Compl. ¶ 62; *Gen. Motors*, 407 B.R. at 473; Ex. K at 3. However, "the primary purpose of the corporate form is to prevent a company's owners, whether they are persons or other corporations, from being liable for the activities of the company." *Cent. States, S.E. & S.W Areas Pension Fund v. Reimer Express World Corp.*, 230 F.3d 934, 944 (7th Cir. 2000). Accordingly, "a company's owners reasonably expect that they cannot be held liable for the faults of the company," so long as the owners do not "exercise an unusually high degree of control over the [company]" and the "corporate formalities have been observed." *See id.* at 943, 944. For these reasons, "[t]he Government may subsidize private entities without assuming constitutional responsibility for their actions." *San Fran. Arts & Ath., Inc. v. U.S. Olympic Comm.*, 483 U.S. 522, 544 (1987).

In this case, the government has taken great pains to maintain Old GM and New GM as entities separate from itself. When the President announced on March 30, 2009, that "[his] team [would] be working closely with [Old] GM [over the next 60 days] to produce a better business plan," he made a point of stating that "the United States Government" had "no interest in running GM" and "no intention of [doing so]." Ex. J at 2. The negotiations that the Auto Task Force conducted with Old GM between March 30 and June 1, 2009, were "[c]ontentious, often difficult, [and] sometimes exasperating," i.e., "intense [and] arms'-length." Ex. L at 181:3-8; *Gen. Motors*, 407 B.R. at 494. When the President announced on June 1, 2009, that a plan had been negotiated that would "give this iconic American company a chance to rise again," he reiterated that "we * * * have no interest in * * * running GM," and underscored that point by saying that "[New] GM [would] be run by a private board of directors and management team"; that "[t]hey – and not the government – [would] call the shots and make the decisions"; and that "[t]he federal government [would] refrain from exercising its rights as a shareholder in all but the most fundamental corporate decisions." Ex. O at 2. Defendant Bloom reiterated the restraint that the government would exercise as a shareholder of New GM in the statement that he made to the Congressional Oversight Panel on July 27, 2009. *See* Ex. I at 7.

In *Brentwood Academy v. Tennessee Secondary School Athletic Ass'n*, 531 U.S. 288 (2001), "a statewide association incorporated to regulate interscholastic athletic competition among public and private secondary schools" was held to have "engage[d] in state action when it enforce[d] a rule against a member school" because 84% of its members were "public schools represented by their officials acting in their official capacity to provide an integral element of secondary public schooling"; because members of the State Board of Education were "assigned ex officio to serve as members of [the association's governing bodies]"; and because "ministerial employees" of the association were "treated as state employees to the extent of being eligible for membership in the state retirement system." *Id.* at 290, 292, 299-300 (internal quotation marks omitted). Nothing similar to *Brentwood* has happened here. Accordingly, no basis exists for plaintiffs' contention that New GM was acting as a government instrumentality under the entwinement test when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE.

B. New GM Did Not Act as a Government Instrumentality Under the State Compulsion Test When It Agreed to Make Supplemental Payments to Certain Retirees of Delphi Represented by UAW, USW, or IUE.

"The state compulsion test requires that a State has 'exercised such coercive power or has provided such significant encouragement, either overt or covert, that the choice must in law be deemed to be that of the State.'" *Vistein*, 342 F. App'x at 127-28 (quoting *Blum v. Yaretsky*, 457 U.S. 991, 1004 (1982)). "More than mere approval or acquiescence in the initiatives of the private party is necessary to hold the State responsible for those initiatives." *Id.* Accordingly, the state compulsion test is not met by the government's entering into a tax-abatement agreement that permits a company to close a plant and terminate certain of its employees if "[n]o state law or any state entity required [the company]" to enter into the agreement, close the plant, or terminate the employees. *Campbell*, 509 F.3d at 784. Neither is the state compulsion test met by the government's "provid[ing] a significant portion of the funding of [a corporation]" if the government does not choose the members of the corporation's board of trustees, does not choose its executive director, does not make "personnel policies or decisions for [the corporation]," and does not play any other role in the corporation's "day-to-day operation." *Wolotsky v. Huhn*, 960 F.2d 1331, 1335, 1336 (6th Cir. 1992).

In this case, plaintiffs allege that New GM acted as a government instrumentality under the state compulsion test when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE because the government was "extensively involved in questions related to the outcome of pension benefits to Delphi's retirees," exerted "significant pressure" on New GM to persuade it to make those payments, and did so "in connection with governmental policies that were politically motivated." *See* 1st Am. Compl. ¶¶ 37, 62. These allegations are unfounded. The issue of "Delphi's pensions" was but one of "thousands of issues" with which the Auto Task Force was required to deal "in an extraordinarily short period of time." *See* Ex. D at 155:9:156:22; Ex. M at 295:13-16. In considering those issues, the Auto Task Force avoided "[u]sing GM * * * as an instrument of broader government policy" because its doing so would have been "inconsistent" with its goal of "promoting [a] strong and viable compan[y], which [could] be profitable and contribute to economic growth and jobs without Government support as quickly as possible." Ex. I at 6. In addition, the Auto Task Force did not dictate what should be done with the Delphi pensions. Although the Auto Task Force anticipated initially that New GM would assume liability for the Delphi hourly plan as a whole, New GM made different arrangements, and the Auto Task Force went along. *See* Ex. D at 159:22-160:2, 176:3-15, 183:5-184:15.

Accordingly, the impetus for New GM's agreeing to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE came from UAW, USW, and IUE, not from the Auto Task Force. "[A]s a matter of reality, [New GM] need[ed] a properly motivated workforce to enable [it] to succeed, requiring it to enter into satisfactory agreements with the UAW – which include[d] arrangements satisfactory to the UAW for UAW retirees." *Gen. Motors*, 407 B.R. at 512. In addition, USW and IUE threatened New GM with "the costs, risks, and delays associated with litigat[ion]" if New GM did not enter into an agreement with USW and IUE to resolve certain "assert[ions]" that they made. Ex. R at 1. For these reasons, UAW, USW, and IUE possessed "negotiating leverage" that made it "commercially necessary and reasonable" for New GM to agree to honor the benefit guarantee agreements into which Old GM had entered at the time of the Delphi spin off. *See* Ex. M at 98:19-100:2, 291:8-16.

In view of the foregoing, New GM did not act as a government instrumentality under the state compulsion test when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE because the Auto Task Force did not "'exercise[] such coercive power'" or "'provide[] such significant encouragement'" that "'the choice must in law be deemed to be that of [the government].'" *See Vistein*, 342 F. App'x at 127-28 (quoting *Blum*, 457 U.S. at 1004). For that reason, this action should be dismissed as to Treasury Defendants.

III. NO DENIAL OF EQUAL PROTECTION, FREEDOM OF ASSOCIATION OR FREEDOM OF SPEECH HAS TAKEN PLACE HERE EVEN ASSUMING, *ARGUENDO*, THAT NEW GM HAS ACTED AS A GOVERNMENT INSTRUMENTALITY.

A. No Denial of Equal Protection Has Taken Place Here.

"Although it contains no Equal Protection Clause as does the Fourteenth Amendment, the Fifth Amendment's Due Process Clause prohibits the Federal Government from engaging in discrimination that is 'so unjustifiable as to be violative of due process.'" *Schlesinger v. Ballard*, 419 U.S. 498, 500 n.3 (1975) (quoting *Bolling v. Sharpe*, 347 U.S. 497, 499 (1954)). In this case, plaintiffs allege that New GM has discriminated against them on the basis of "their decision not to associate with a union" by agreeing to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE, but not to them. 1st Am. Compl. ¶ 60. Based on that allegation, plaintiffs allege that New GM has denied them equal protection. *Id.* For two reasons, plaintiffs are mistaken even assuming, *arguendo*, that New GM acted as a government instrumentality when it agreed to make those payments.

First, the criterion that New GM has used in deciding which retirees of Delphi should receive supplemental payments has not been whether a particular retiree made a decision to "associate with a union." *See* 1st Am. Compl. ¶ 60. Instead, the criterion that New GM has used has been whether a particular retiree was covered by one of the benefit guarantee agreements into which Old GM entered with UAW, USW, or IUE at or about the time of the spin off of Delphi from Old GM in 1999. Accordingly, New GM has not agreed to make supplemental payments to any retiree of Delphi represented by the International Association of Machinists, International Brotherhood of Electrical Workers, certain locals of the Michigan Regional Council of Carpenters, International Brotherhood of Teamsters, International Brotherhood of Boilermakers, IUOE, or United Catering Workers. *See* Ex. R ¶¶ 1(a), 5(a). Neither has New GM agreed to make supplemental payments to any retiree of Delphi represented by UAW, USW, or IUE unless that retiree had "unbroken seniority and [was] employed by [Old] GM under the terms of the [then-current national agreement between Old GM and UAW, USW, or IUE] as of the spin-off of Delphi from [Old] GM on May 28, 1999." *See* Ex. B, Ex. 99.2 at 1, Ex. 99.4 at 1, Ex. 99.5 at 1.

Second, neither "union members" nor "non-union members" are "protected class[es] for purposes of equal protection analysis." *Hoke Co. v. TVA*, 854 F.2d 820, 828 (6th Cir. 1988). Accordingly, government action based on union membership need only be "'rationally related to a legitimate governmental interest'" in order to withstand equal protection scrutiny. *Henry v. Metro. Sewer Dist.*, 922 F.2d 332, 341 (6th Cir. 1990) (quoting *Hoke*, 854 F.2d at 828) (internal quotation marks omitted). "This standard of review is typically quite deferential." *Lyng v. UAW*, 485 U.S. 358, 370 (1988). Accordingly, "the relevant inquiry for [a] court in reviewing [an] equal protection claim [under the rational basis standard] is whether an impartial lawmaker could logically believe that the [challenged] classification would serve a legitimate public purpose that transcends the harm to the members of the disadvantaged class." *Hoke*, 854 F.2d at 829. In addition, the application of the rational basis standard does not require the defendant to "offer any rational basis" for the challenged classification "so long as as th[e] Court can conceive of one." *Club Italia*, 470 F.3d at 299. As a result, "the burden falls entirely to [the] Plaintiff to show there is no rational basis, not the other way around." *Id.*

In this case, plaintiffs allege that the decision of New GM to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE but not to plaintiffs is not "support[ed]" by any "relevant extenuating circumstances." 1st Am. Compl. ¶¶ 59, 60. Plaintiffs are mistaken. The possibility of collapse that Old GM and Chrysler faced in December 2008 threatened the economy of the United States with "a potentially crippling blow," i.e., the possible elimination of "nearly 1.1 million jobs." Ex. F at 3. The plans to "restructure, to modernize, and to make themselves more competitive" that Old GM and Chrysler submitted to the government in February 2009 did not "go[] far enough to warrant the substantial new investments that these companies [were] requesting." Ex. J at 1. Because the government could not "let our auto industry simply vanish," both companies were offered "a limited additional period of time to work with creditors, unions, and other stakeholders to fundamentally restructure in a way that would justify an investment of additional taxpayer dollars." *Id.*. After speaking to "dozens of experts, advisors, consultants, industry experts, who collectively had thousands of years of experience in the automotive industry, as well as, obviously, the management team at great length," the Auto Task Force concluded that the only way to achieve "[Old GM's] primary goals and [UST's] primary goals of having a viable GM" was for Old GM to file a petition for reorganization under Chapter 11 of the Bankruptcy Code and to move for an order under §363 of the Bankruptcy Code permitting the sale of the assets of Old GM to a "Treasury-sponsored entity," New GM. *See* Ex. L at 182:19-183:11, 192:16-17; Ex. M at 14:1-15:21. A sale under § 363 offered the possibility of "speed, certainty and the ability to leave behind liabilities that a commercial buyer would not want to have in the new company." Ex. M at 120:18-25. Accordingly, the aim of the Auto Task Force in negotiating the details of the proposed sale under § 363 was to structure a transaction in which New GM would assume only those liabilities of Old GM that were "commercially necessary," i.e., necessary "in order for [New GM] to operate." *See id.* at 263:20-23, 276:22-277:8, 291:10-16, 294:2-10, 302:16-19; Ex. L at 102:25-103:2, 111:23-25, 135:16-22.

In this case, Old GM entered into benefit guarantee agreements with UAW, USW, and IUE at or about the time of the Delphi spin off in 1999 that obligated it under certain circumstances to pay supplemental benefits to certain retirees of Delphi represented by UAW, USW, or IUE. *See* Ex. B, Ex. 99.2 ¶ (e), Ex. 99.4 ¶ (e), Ex. 99.5 ¶ (e). However, Old GM never became obligated under any circumstance to make supplemental payments to any other retiree of Delphi, including any retiree who had been a salaried employee of Delphi. New GM "need[ed] a properly motivated workforce to enable [it] to succeed." *See Gen. Motors*, 407 B.R. at 512. In addition, New GM wished to avoid "the costs, risks and delays associated with litigating" its alleged obligation to retirees represented by USW and IUE. *See* Ex. R at 1. Accordingly, New GM had solid commercial reasons to agree to make supplemental payments to those retirees of Delphi, represented by UAW, USW, or IUE, who came within the purview of the benefit guarantee agreements. However, New GM never had any reason "in triaging its expenditures" to agree to make supplemental payments to other retirees of Delphi, including plaintiffs. *See Gen. Motors*, 407 B.R. at 512. Accordingly, the exclusion of plaintiffs from the universe of retirees of Delphi to whom New GM has agreed to make supplemental payments was, and is, a permissible action under the rational basis test. Plaintiff's equal protection claim should therefore be dismissed even assuming, *arguendo*, that New GM acted as a government instrumentality when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, IUE.

B. No Denial of Freedom of Association Has Taken Place Here.

Government action that does not "'directly and substantially interfere'" with the "ability [of employees] not to associate in a union" does not deprive them of their right to freedom of association. *Hoke*, 854 F.2d at 828 (quoting *Lyng*, 485 U.S. at 366). Accordingly, the government does not deprive the employees of a non-unionized company of their right to freedom of association by awarding a contract for the purchase of goods to a unionized company because the awarding of the contract does not "require an exaction from any individual, coerce any belief, or require [the] employees to become unionized." *Id.* In the same way, the granting of "exclusive privileges" to a union that represents the majority of an agency's employees does not "in any way impair the independent rights of other groups of [employees] to exercise their First Amendment rights in the context of the [work] setting." *Memphis Am. Fed'n of Teachers v. Bd. of Educ.*, 534 F.2d 699, 702 (6th Cir. 1976).

On the theory that New GM acted as a government instrumentality when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE, plaintiffs allege that New GM has "unconstitutionally burdened [their] right to choose freely how and with whom to associate" by "inject[ing] undue favoritism into private labor relationships." 1st Am. Compl. ¶ 60. Even assuming, *arguendo*, that the "injection of undue favoritism into private labor relationships" violates the Constitution, no such injection of "undue favoritism" has taken place here.[10] The sole retirees of Delphi to whom New GM has agreed to make supplemental payments are certain retirees of Delphi who had "unbroken seniority and were employed by [Old] GM under the terms of the [then-current national agreement between Old GM and UAW, USW, or IUE] as of the spin-off of Delphi from [Old] GM on May 28, 1999." *See* Ex. B, Ex. 99.2 at 1, Ex. 99.4 at 1, Ex. 99.5 at 1. Accordingly, plaintiffs could not make themselves eligible for the supplemental payments that New GM has agreed to make to certain retirees of Delphi represented by UAW, USW, or IUE by joining UAW, USW, or IUE today. In view of that fact, New GM has not given plaintiffs any incentive to join UAW, USW, or IUE, much less interfered in any "'direct[] or substantial'" way "with [their] ability not to associate in a union." *See Hoke*, 854 F.2d at 828 (quoting *Lyng*, 485 U.S. at 366). Plaintiffs' freedom of association claim should therefore be dismissed.

C. No Denial of Freedom of Speech Has Taken Place Here.

On the theory that New GM acted as a government instrumentality when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE, plaintiffs allege that its having agreed to do so has violated the "speech guarantees" of the First Amendment. 1st Am. Compl. ¶ 60. However, plaintiffs do not explain how New GM's having agreed to make those payments has violated any such guarantees. *See id.* Nor would any such explanation be persuasive. "'[A]bove all else, the First Amendment means that government has no power to restrict expression because of its message, its ideas, its subject matter, or its content."

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[10] In *Lyng v. UAW*, 485 U.S. 360 (1988), a statute was held to withstand scrutiny under the "equal protection component of the Due Process Clause" because the statute was "rationally related to the legitimate governmental objective of avoiding undue favoritism to one side or the other in private labor disputes" 485 U.S. at 364, 371. No "private labor dispute[]" is implicated here.

Memphis Am. Fed'n Teachers, 534 F.2d at 702 (quoting *Police Dep't of Chicago v. Mosley*, 408 U.S. 92, 95 (1972)). However, the right of individuals to "express themselves about union matters free of coercion by the Government" is not abridged by government action that "requires no exaction from any individual"; "does not 'coerce' belief" about union matters; and does not require individuals to "participate in political activities or support political views with which they disagree." *Lyng*, 485 U.S. at 369. In this case, the agreement of New GM to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE does none of these things. Plaintiffs' freedom of speech claim should therefore be dismissed.

IV. PLAINTIFFS ARE NOT ENTITLED TO AN ORDER DIRECTING TREASURY DEFENDANTS TO PROVIDE FURTHER LOAN ASSISTANCE TO NEW GM OR AN AWARD OF DAMAGES AGAINST DEFENDANTS GEITHNER, RATTNER, OR BLOOM.

A. Plaintiffs Are Not Entitled to an Order Directing Treasury Defendants to Provide Further Loan Assistance to New GM.

"[P]ayments of money from the Federal Treasury are limited to those authorized by statute." *OPM v. Richmond*, 496 U.S. 414, 416 (1990). Accordingly, it is "'the duty of all courts to observe the conditions defined by Congress for charging the public treasury.'" *Id.* at 420 (quoting *Fed. Crop. Ins. Corp. v. Merrill*, 332 U.S. 380, 385 (1947)). Because of that duty, "it would be most anomalous for a judicial order to require a Government official * * * to make an extrastatutory payment of federal funds." *Id.* at 430.

These principles apply to cases, like this one, in which constitutional claims are asserted. "[E]ven where the Constitution prohibits coercive governmental interference with specific individual rights, it 'does not confer an entitlement to such funds as may be necessary to realize all the advantages of that freedom.'" *Lyng*, 485 U.S. at 369 (quoting *Regan v. Taxation With*

Rep., 461 U.S. 540, 550 (1983)). Accordingly, "'a legislature's decision not to subsidize the exercise of a fundamental right does not infringe the right'" even if a particular group "would be much better off" if the right were subsidized. *Id.* at 368 (quoting *Regan*, 461 U.S. at 549); *see Hoke*, 854 F.2d at 829 (similarly).

In this case, plaintiffs seek certain "specific relief" if the Court finds that the agreement of New GM to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE has denied them equal protection, freedom of association, or freedom of speech. 1st Am. Compl. ¶ 61. The relief that plaintiffs seek includes an order directing Treasury Defendants to direct New GM to "'top-up' the Salaried Plan in the same manner as it [allegedly] is topping up the union-affiliated plans, providing additional loan assistance to New GM if necessary." *Id.* ¶ 61(a). However, plaintiff's request for an order directing Treasury Defendants to "provid[e] additional loan assistance to New GM if necessary" presupposes that plaintiffs have "'an entitlement to such funds as may be necessary'" to remedy the denial of equal protection, freedom of association, and free speech that they allege. *See Lyng*, 485 U.S. at 368 (quoting *Regan*, 461 U.S. at 550). Plaintiffs have no such "'entitlement,'" *see id.*, and the Court has no authority to give them one. *See Richmond*, 496 U.S. at 421. Accordingly, plaintiffs are not entitled to an order directing Treasury Defendants to "provid[e] additional loan assistance to New GM" even assuming, *arguendo*, that any denial of equal protection, freedom of association, or freedom of speech has taken place here.

B. Plaintiffs Are Not Entitled to an Award of Damages Against Defendants Geithner, Rattner, or Bloom.

In *Bivens v. Six Unknown Named Agents of the Federal Bureau of Narcotics*, 403 U.S. 388 (1971), the Supreme Court "'recognized for the first time an implied private action for damages against federal officers alleged to have violated a citizen's constitutional rights.'" *Ashcroft v. Iqbal*, 129 S. Ct. 1937, 1947 (2009) (quoting *Corr. Serv. Corp. v. Malesko*, 534 U.S. 61, 66 (2001)). In this case, plaintiffs allege that they are entitled to an award of compensatory and punitive damages against defendants Geithner, Rattner, and Bloom under *Bivens* because the agreement of New GM to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE has denied them equal protection. *See* 1st Am. Compl. ¶ 64. However, the *Bivens* claim that plaintiffs seek to assert against defendants Geithner, Rattner, and Bloom is precluded by statute; fails to state a claim upon which relief can be granted; and is barred by the doctrine of qualified immunity. For all of those reasons, the claim should be dismissed.

1. The *Bivens* Claim That Plaintiffs Seek to Assert Against Defendants Geithner, Rattner, and Bloom Is Precluded by Statute.

Claims under *Bivens* are precluded by statute in cases where "Congress has put in place a comprehensive system to administer public rights, has 'not inadvertently' omitted damages remedies for certain claimants, and has not plainly expressed an intention that the courts preserve *Bivens* remedies." *Spagnola v. Mathis*, 859 F.2d 223, 228 (D.C. Cir. 1988) (en banc) (paraphrasing *Schweiker v. Chilicky*, 487 U.S. 412, 423 (1988)). In such cases, "[i]t is the comprehensiveness of the statutory scheme involved, not the 'adequacy' of specific remedies extended thereunder, that counsels judicial abstention." *Id.* at 227. In accordance with these principles, the Supreme Court has "declined to recognize a *Bivens* claim involving the social security system, given the existence of a mechanism for the resolution of claims," and other courts have held that "*Bivens* claims are not available in tax-related disputes because Congress has created a comprehensive statutory scheme which provides alternative remedies for the types of wrongs that may otherwise be the subject of a *Bivens* claim." *Hook v. United States*, 2008 WL 4424811, at *8 (D. Colo. Sept. 25, 2008).

In this case, plaintiffs contest the agreement of New GM to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE. However, New GM has agreed to make those payments as part of the restructuring of Old GM under the Bankruptcy Code. *See* Ex. D at 156:10-22, 161:15-162:15, 176:3-12: Ex. R at 1. Like the Tax Code, the Bankruptcy Code is "a comprehensive statutory scheme which provides alternative remedies for the types of wrongs that may otherwise be the subject of a *Bivens* claim." *See Hook*, 2008 WL 4424811. Accordingly, the *Bivens* claim that plaintiffs seek to assert against defendants Geithner, Rattner, and Bloom is precluded by statute.

2. The *Bivens* Claim That Plaintiffs Seek to Assert Against Defendants Geithner, Rattner or Bloom Fails to State a Claim Upon Which Relief Can Be Granted.

"The factors necessary to establish a *Bivens* violation * * * vary with the constitutional provision at issue." *Iqbal*, 129 S. Ct. at 1948. Where, as here, a *Bivens* claim is based on an alleged denial of equal protection, "the plaintiff must plead and prove that the defendant acted with discriminatory purpose." *Id.* "[P]urposeful discrimination requires more than 'intent as volition or intent as awareness of consequence.'" *Id.* (quoting *Personnel Adm'r v. Feeney*, 442 U.S. 256, 279 (1979)). "It instead involves a decisionmaker's undertaking a course of action 'because of, not merely in spite of, [the action's] adverse effects upon an identifiable group.'" *Id.* Accordingly, a plaintiff who wishes to state a claim under *Bivens* "must plead sufficient factual material" to show that an act of alleged discrimination was committed "for the purpose of discriminating," not merely for a "neutral" reason. *See id.* at 1948-49.

In this case, plaintiffs plead no "factual material" suggesting that defendants Geithner, Rattner, or Bloom have taken any action at any time "for the purpose of discriminating" against salaried retirees of Delphi, either because of "their decision not to affiliate with a union" or for any other reason. *See Iqbal*, 129 S. Ct. at 1948-49; 1st Am. Compl. ¶ 60. Accordingly, plaintiffs have failed to state a claim under *Bivens* against any of those defendants. *See Iqbal*, 129 S. Ct. at 1948-49.

3. The *Bivens* Claim That Plaintiffs Seek to Assert Against Defendants Geithner, Rattner, and Bloom Is Barred by the Doctrine of Qualified Immunity.

Suing government officials under *Bivens* "exacts heavy costs in terms of efficiency and expenditure of valuable time and resources that might otherwise be directed to the proper execution of the work of the Government." *Iqbal*, 129 S. Ct. 1953. Accordingly, "[t]he doctrine of qualified immunity affords protection against individual liability for civil damages to officials 'insofar as their conduct does not violate clearly established statutory or constitutional rights of which a reasonable person would have known.'" *Henry*, 922 F.2d at 339 (quoting *Harlow v. Fitzgerald*, 457 U.S. 800, 818 (1982)). The need for qualified immunity is particularly acute where, as here, officials are accused of having violated the Consitution while responding to a national or international emergency "unprecedented in the history of the American Republic." *See Iqbal*, 129 S. Ct. at 1953 (internal quotation marks omitted).

"A court evaluating a claim of qualified immunity 'must first determine whether the plaintiff has alleged the deprivation of an actual constitutional right at all and, if so, proceed to determine whether that right was clearly established at the time of the alleged violation.'" *Wilson v. Layne*, 526 U.S. 603, 609 (1999) (quoting *Conn v. Gabbert*, 526 U.S. 286, 290 (1999)). "This order of procedure is designed to 'spare a defendant not only unwarranted liability, but unwarranted demands customarily imposed upon those defending a long drawn out lawsuit.'" *Id.* (quoting *Seigert v. Gilley*, 500 U.S. 226, 232 (1991)). If required, the second phase of analysis "'generally turns on the objective legal reasonableness of the [allegedly unlawful official action], assessed in light of the legal rules that were clearly established at the time it was taken.'" *Id.* at 614 (quoting *Anderson v. Creighton*, 483 U.S. 635, 639 (1987)) (internal quotation marks omitted). For purposes of the second phase of analysis, "'[t]he contours of the right must be sufficiently clear that a reasonable official would understand that what he is doing violates that right.'" *Id.* (quoting *Anderson*, 483 U.S. at 640). "'This is not to say that an official action is protected by qualified immunity unless the very action in question has previously been held unlawful, but it is to say that in the light of pre-existing law the unlawfulness must be apparent.'" *Id.*

In this case, defendants Geithner, Rattner, and Bloom are entitled to qualified immunity for two reasons. First, plaintiffs have not been "'depriv[ed] of an actual constitutional right.'" *See Wilson*, 526 U.S. at 609 (quoting *Conn*, 526 U.S. at 290). No denial of equal protection has taken place here because New GM was not acting as a government instrumentality when it agreed to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE; because the criterion that New GM has used in deciding which retirees of Delphi should receive supplemental payments has not been whether a particular retiree made a decision to "associate with a union"; and because the exclusion of plaintiffs from the universe of retirees of Delphi to whom New GM has agreed to make supplemental payments was, and is, a permissible action under the rational basis test. *See* Points II, III(A), *supra*.

Second, the "'legal rules'" that were "'clearly established'" at the time that New GM agreed to make the supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE would not have made it "'apparent'" to a "'reasonable official'" that the agreement of New GM constituted a denial of equal protection. *See Wilson*, 526 U.S. at 614 (quoting *Anderson*, 483 U.S. at 639, 640). To the contrary, the "'legal rules'" that were "'clearly established'" at the time of the agreement would have suggested that the agreement constituted no such a denial. Those rules were established by cases like *Lyng v. UAW*, 485 U.S. 360 (1988). In *Lyng*, certain unions and union members alleged that they were denied equal protection by a statute prohibiting any household from "becom[ing] eligible to participate in the food stamp program during the time that any member of the household [was] on strike" or from "increas[ing] the allotment of food stamps that it was receiving already because the income of the striking member ha[d] decreased." 485 U.S. at 362. Finding that the statute possessed a rational basis that precluded its invalidation, the Court held that "protecting the fiscal integrity of Government programs, and of the Government as a whole, 'is a legitimate concern of the State'"; that judicial review "of distinctions that Congress draws in order to make allocations from a finite pool of resources must be deferential, for the discretion about how best to spend money to improve the general welfare is lodged in Congress rather than the courts"; and that "'[f]iscal considerations may compel certain difficult choices in order to improve the protection afforded to the entire benefited class.'" *Id.* at 373 (quoting *Ohio Bureau of Empl. Serv. v. Hodory*, 431 U.S. 471, 493 (1977) & *Harris v McRae*, 448 U.S. 448 U.S. 297, 355 (1980) (Stevens, J., dissenting)).

In this case, the agreement of New GM to make supplemental payments to certain retirees of Delphi represented by UAW, USW, or IUE, but not to make supplemental payments to other retirees of Delphi, possessed "'objective legal reasonableness'" under "'the legal rules that were clearly established'" at the time of the agreement because New GM was a company with a "finite pool of resources" and because its "fiscal integrity" had to be "protect[ed]" if it was to have any "long-term prospect[] for success." *See Wilson*, 526 U.S. at 614 (quoting *Anderson*, 483 U.S. at 639) (internal quotation marks omitted); *Lyng*, 485 U.S. at 373; Ex. J at 1. Accordingly, this case is one in which "'[f]iscal considerations * * * compel[led] certain difficult choices in order to improve the protection afforded to the entire benefited class.'" *See Lyng*, 485 U.S. at 373 (quoting *Harris*, 448 U.S. at 355). In view of these facts, the doctrine of qualified immunity would shield defendants Geithner, Rattner, and Bloom from liability under *Bivens* even assuming, *arguendo*, that any denial of equal protection took place here.

CONCLUSION

For the foregoing reasons, the motion of Treasury Defendants to dismiss or, in the alternative, for summary judgment should be granted.

Respectfully submitted,

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Dated: February 16, 2010

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

DENNIS BLACK, *et al.*, Plaintiffs, v. PENSION BENEFIT GUARANTY CORPORATION, *et al.*, Defendants.	No. 2:09-cv-13616-AJT-DAS [PROPOSED] ORDER

Upon the motion of defendants U.S. Department of the Treasury, the Presidential Task Force on the Auto Industry, Timothy F. Geithner, Steven L. Rattner, and Ron A. Bloom (Treasury Defendants) to dismiss or, in the alternative, for summary judgment, the materials submitted in support thereof and in opposition thereto, and good cause having been shown, it is hereby ordered as follows:

1. The aforementioned motion of Treasury Defendants is hereby granted.
2. This action is hereby dismissed as to Treasury Defendants.

Date: ____________________

____
UNITED STATES DISTRICT JUDGE

SIGTARP OFFICE OF THE SPECIAL INSPECTOR GENERAL FOR THE TROUBLED ASSET RELIEF PROGRAM

ADVANCING ECONOMIC STABILITY THROUGH TRANSPARENCY, COORDINATED OVERSIGHT AND ROBUST ENFORCEMENT

FOR OFFICIAL USE ONLY UNTIL RELEASED BY THE
HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

QUESTIONS FOR THE RECORD FROM NEIL BAROFSKY

SPECIAL INSPECTOR GENERAL
FOR THE TROUBLED ASSET RELIEF PROGRAM

FROM JANUARY 27, 2010 HEARING

March 12, 2010

QUESTION FOR MR. BAROFSKY

By Ranking Member Bachus, Committee on Financial Services, participating by unanimous consent of the Committee:

1. In preparing your November 2009 Audit of the AIG counterparty payments, were you aware of the November 5, 2008 BlackRock presentation that was widely reported in the media on January 26, 2009, which clearly showed that Goldman Sachs was willing to tear up its CDS contracts with AIG, which would have saved the taxpayers billions? Why was the information contained in the BlackRock report withheld from your November audit of the AIG counterparty payment issue?

Answer:

SIGTARP did receive the Blackrock Solutions presentation dated November 5, 2008, and reviewed it as part of the audit process. Notwithstanding what may have been implied in media reports, the presentation does not suggest that Goldman Sachs would have been willing to tear up its CDS contracts with AIG, at least not without receiving huge payments of billions of dollars in return, and even then, under terms far different (and less advantageous to AIG and the Federal Reserve) than the structure of the Maiden Lane III transactions.

The Blackrock Solutions presentation provided certain background information concerning the AIG counterparties' CDS positions in anticipation of the FRBNY's discussions with those counterparties, which occurred on November 6 and 7, 2008. The presentation, on page 12 (bates label FRBNYAIG00188), among other things, contains brief bullet point discussions of the following:

- <u>Goldman Sachs' Negotiations with AIG in August 2008</u>: The presentation contained a brief discussion about AIG's negotiations with Goldman Sachs that occurred in August 2008, noting that Goldman Sachs was "the only counterparty willing to tear up CDS with AIG at agreed upon prices and retain CDO exposure." The presentation goes on to note, however, that the difference between what AIG was willing to pay and what Goldman Sachs was willing to accept in exchange for tearing up the CDS contracts was $300 million. This transaction did not contemplate AIG receiving the underlying CDOs.

- <u>Blackrock Solutions' View About Goldman Sachs' Willingness to Accept a Concession</u>: The presentation goes on to speculate that Goldman Sachs "would likely accept a small concession . . ." in connection with the Maiden Lane III transaction. It proceeds, however, to note that Goldman Sachs' exposure to AIG was limited to the difference between what Goldman Sachs had requested in collateral and what had been posted by AIG, and that the cost to hedge against this exposure would be, at most, 2% of the Goldman Sachs CDS portfolio.

As events unfolded, neither of these issues had much impact on the actual negotiations. First, the negotiations between AIG and Goldman Sachs in August related to a different transaction than the FRBNY's negotiations with Goldman Sachs in connection with Maiden Lane III in

November. In August, AIG explored making a payment to Goldman Sachs in return for tearing up the CDS contracts in which Goldman Sachs would *retain* the underlying collateralized debt obligations ("CDOs") — in other words, Goldman Sachs would agree to a large payout in cash in return for relieving AIG of any responsibility to make future payments on the CDSs, but Goldman Sachs would still keep the underlying CDO assets. According to the Blackrock Solutions presentation, the parties were still $300 million apart even for this more limited transaction. The November negotiations, on the other hand, were very different for two reasons: one, the basic economic terms were different, because the Maiden Lane III transactions (unlike the August discussions) included not only the termination of the CDSs, but also the transfer of the underlying CDOs (worth, in total, tens of billions of dollars) to the Federal Reserve —— thus significantly changing the calculus related to giving concessions; two, by November, the Federal Reserve had already bailed out AIG and provided AIG with billions of dollars which it then transferred to Goldman Sachs and the other counterparties in the form of additional collateral payments, which, according to both the Federal Reserve and Goldman Sachs, had a significant impact on the relative negotiation positions.

Second, the Blackrock Solutions' opinion that Goldman Sachs would likely agree to a small (2% or less) concession turned out to be incorrect. As set forth in our audit report, FRBNY and Goldman Sachs both told SIGTARP in interviews that during the negotiating process Goldman Sachs indicated that it was unwilling to accept any concession in connection with the Maiden Lane III transactions, and that while FRBNY sought modest concessions from each of the largest counterparties, including Goldman Sachs, and only one, UBS, was willing to agree to a small concession (again, 2%) and only if all of the others did as well. In the final analysis, in determining what information merited inclusion in the audit report, we determined that Blackrock Solutions' inaccurate speculation as to what Goldman Sachs' negotiation position might have been did not merit inclusion in the audit, particularly given the relatively small size of the concession anticipated in the Blackrock Solutions report.

That does not mean, of course, that a different negotiation strategy and/or different level of effort in trying to obtain concessions from the counterparties could not have potentially obtained a better result for taxpayers. As detailed in the audit and in my testimony before the Committee, in pursuing the November negotiations, FRBNY made several policy decisions which we believe unnecessarily limited the ability of FRBNY to pursue a successful negotiations strategy, and that the half-hearted effort that FRBNY put into the actual negotiations themselves all but ensured their failure.

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April 8, 2010

The Honorable Marcy Kaptur
9th District, Ohio
Committee on Oversight and Government Reform
2157 Rayburn House Office Building
Washington, D.C. 20515-6143

Dear Representative Kaptur:

We write on behalf of former Treasury Secretary Henry M. Paulson in response to the questions submitted on your behalf in connection with the January 27, 2010 AIG hearing. A copy of the text of your questions is attached to this letter.

Question 1 asks what position Mr. Paulson held before being appointed to serve as Secretary of the Treasury. Before becoming Secretary of the Treasury, Mr. Paulson was the Chief Executive Officer of Goldman Sachs.

Questions 2, 3, and 4 ask about the personnel of Goldman Sachs, the White House, and Treasury respectively, and should be directed to those entities.

Question 5 asks Mr. Paulson to recall certain communications between him and then FRBNY President Timothy Geithner during the Fall of 2008 relating to AIG. Mr. Paulson testified at the hearing that he had two conversations with Secretary Geithner concerning AIG over the weekend of September 13, 2008. *See* Hr'g Tr. at 63. In his book, Mr. Paulson recounts several calls with Secretary Geithner on September 16, 2008 concerning AIG. *See* Paulson, Henry M., *On the Brink*, at 229, 235, 239. In his book Mr. Paulson also recounts a conversation with Secretary Geithner on October 14, 2008, concerning AIG. *See id.* at 276.

Question 6 assumes that Secretary Paulson "use[d] Goldman Sachs to give the Treasury advice on AIG," which is not the case.

Question 7 concerns the NYFRB's monitoring of AIG and so should be directed to the NYFRB.

Question 8 refers to "contingency plans for a run on AIG." Question 9 refers to a "liason with AIGFP's regulator UK's FSA." We do not know what is being referred to by those questions.

Questions 10 through 18 concern the payments to certain AIG counterparties. As Mr. Paulson testified at the hearing, he had no involvement with those decisions. *See* Hr'g Tr. at 53.

Question 19 asks about the relationship between the Secretary of the Treasury and the Federal Reserve Bank of New York. The Federal Reserve Bank of New York is part of the Federal Reserve System and is one of the twelve Reserve Banks created by Congress under the Federal Reserve Act of 1913. Supervision and control of the FRBNY are exercised by a board of directors, three appointed by the Board of Governors of the Federal Reserve System and six elected by member banks. *See* 2008 Annual Report of the FRBNY (available at http://www.newyorkfed.org/aboutthefed/annual/annual08/annual.pdf).

Question 20 asks whether an October 8, 2008 letter from Secretary Paulson to then FRBNY President Geithner concerns the "Maiden Lane facilities." It does not; the letter refers to an earlier loan made to AIG, which Mr. Paulson referenced on page one of his written testimony to the Committee.

Very truly yours,

Kevin M. Downey

Enclosure

Committee on Oversight and Government Reform
Questions for the Record
Hearing: January 27, 2009 - "The Federal Bailout of AIG"

QUESTIONS FOR MR. HENRY PAULSON

By Representative Marcy Kaptur:

1. Who did you work for what position did you hold before being appointed by President Bush to serve as Secretary of the Treasury?

2. To your knowledge, did any relative of President Bush ever work at Goldman Sachs while you were Secretary of the Treasury, and if so, who and in what capacity?

3. To your knowledge, did any one serving in the White House ever work at ever work at Goldman Sachs while you were Secretary of the Treasury, and if so, who and in what capacity?

4. When you were Secretary of the Treasury, how many people worked in the Department of Treasury who had worked at Goldman Sachs?

5. In the phone logs of Secretary Geithner from Sept. 14 to Dec.31, 2008, when he was President of the Federal Reserve Bank of New York, it shows that he called you well over 200 times. How many of those conversations were about AIG, and when?

6. Why did you use Goldman Sachs to give the Treasury advice on AIG given that Goldman Sachs had a major conflict of interest as a counter party to AIG through CDS's?

7. What monitoring of AIG's exposure to CDS written on CDOs did NY Fed undertake in
   a. 2004-2006
   b. H1 2007 after HSBC mortgage blowup
   c. H2 2007 after Bear Stearn Hedge Fund blowup
   d. Q1 2008 after monoline distress
   e. Q2 2008 after Bear blowup and acute monoline distress
   f. Q3 2008 in run up to collateral calls on AIG?

   (subject to result of above questions). The following blog entry, by an anonymous securities lawyer familiar with the terrain, criticises a financial journalist for obliviousness to the level of risk at AIG in mid-2007, pointing to a widely distributed Fitch report that highlight's AIG's exposure. AIG was well known as a major, if not the major, credit default swaps counterparty. Certainly by the time of the Bear Stearns rescue, if not sooner, credit default swaps were recognized as a source of systemic risk; if nothing else, Eric Dinallo of New York State Deptment of Insurance made that clear in January 2008. Why was there no interest in AIG as a source of counterparty risk to the dealer community? http://economicsofcontempt.blogspot.com/2009/09/risk-held-at-aigfp-was-not-surprise.html

8. On what date did Treasury start making contingency plans for a run on AIG? What the NYFRB involved?

9. On what date did Treasury begin liaison with AIGFP's regulator UK's FSA? What the NYFRB involved?

10. On what date did Treasury start the process of discovering who AIG's counterparties were for the CDS's written on CDO's by AIG? What the NYFRB involved?

11. What risk modeling or other assessments did Treasury undertake of the resulting systemic risk and when did they start? What the NYFRB involved?

12. What legal advice did Treasury take regarding the prospect of successfully challenging the French claim that settling the AIG CDS on CDOs for 100 cents on the dollar would be illegal under Franch law?

13. Is it correct that you claimed at the time that legal obstacles faced by the French banks were a major reason why haircuts could not be negotiated?

14. Are you aware that it has since become clear that those legal difficulties were fictitious?

15. Considering how Socgen and Calyon were both very closely linked to US banks in particular, over half of SocGen's exposure was underwritten by Goldman, for example], is it possible that US banks knew about or encouraged French banks to urge their regulators to represent their legal situation falsely? Do you think an investigation might be warranted?

16. Some of the owners of the CDOs purchase by Maiden Lane III were not the banks, but their clients. They are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance? Who were the third party clients of Goldman (and others?) who benefited from the Maiden Lane III payments to Goldman? Was any investigation performed to determine who they were and whether they were appropriate recipients of taxpayer payments? Were any conflicts of interest investigated with respect to such payments?

17. What's the propriety of the taxpayers, via our subsidy to AIG, paying UBS $5 billion while the Justice Department was prosecuting it for massive tax fraud?

18. What's the propriety of the taxpayers, via our subsidy to AIG, paying UBS $5 billion while the Justice Department was prosecuting it for massive tax fraud?

19. As the Secretary of the Treasury, what, if any power did you have over the Federal Reserve Bank of New York and its Wall Street members?

20. Mr. Paulson, the Oversight and Government Reform Committee has obtained a document from you as Secretary of the Treasury to then President of the Federal Reserve Bank of New York President, Mr. Geithner dated October 8, 2008. In the letter you state that you believed that the Federal Reserve Bank of New York's provision of a special liquidity facility to AIG in order to allow the company to meet its obligations was necessary to prevent the substantial disruption of to financial markets and the economy that could well have occurred from a disorderly wind-down of AIG.

    Mr. Paulson – I assume that these are the Maiden Lane facilities and that these facilities allowed the counterparties to be paid in full. Is that correct?

    As the Secretary of the Treasury, what, if any power did you have over the Federal Reserve Bank of New York and its Wall Street members?

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EDWARD BENNETT WILLIAMS (1920-1988)
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April 8, 2010

The Honorable Mark Souder
3rd District, Indiana
Committee on Oversight and Government Reform
2157 Rayburn House Office Building
Washington, D.C. 20515-6143

Dear Representative Souder:

We write on behalf of former Treasury Secretary Henry M. Paulson in response to the question submitted on your behalf in connection with the January 27, 2010 AIG hearing.

You asked Secretary Paulson to: "Please explicitly define how you measure systemic risk."

Secretary Paulson's view is that there is no simple measure of systemic risk. Whether, and to what extent, an institution poses a systemic risk depends on the overall condition of the financial system and capital markets at a given time as well as on the firm-specific characteristics of the particular institution, such as its size and interconnectedness. The key question in evaluating systemic risk is whether the combination of these factors gives rise to a situation in which the failure of one institution can damage the financial system in a way that causes significant harm to the overall economy.

In light of the difficulty in establishing a precise, uniform measure of systemic risk, Secretary Paulson's view is that two regulatory reforms are needed. First, there should be a systemic risk regulator that can design and implement appropriate systemic risk metrics, monitor the stability of the markets, and restrain activity at any financial firm that threatens the system. Second, because such a regulator will inevitably be unable to foresee and forestall all systemic problems, the government should also have resolution authority to impose an orderly

WILLIAMS & CONNOLLY LLP

The Honorable Mark Souder
April 8, 2010
Page 2

liquidation on any failing financial institution to mitigate the harm to the system occasioned by such a failure.

Mr. Paulson has addressed these issues in more detail in a recent article in the New York Times, a copy of which is enclosed. He has also discussed these issues in his book, *On the Brink*.

Very truly yours,

Kevin M. Downey

Enclosure

The New York Times

February 16, 2010

OP-ED CONTRIBUTOR

How to Watch the Banks

By HENRY M. PAULSON Jr.

Washington

SIXTEEN months ago, our financial system teetered on the brink of collapse. The Treasury, the Federal Reserve and the Federal Deposit Insurance Corporation took actions that were unpopular and previously unthinkable — but absolutely necessary to stave off an economic catastrophe in which unemployment could have exceeded the 25 percent level of the Great Depression.

These temporary actions have ended or will end. And our financial system is much more stable. But it is critical that we learn from the financial crisis and put in place reforms to avert a repeat of 2008 or something even worse.

Congress must pass financial regulatory reform. Delays are creating uncertainty, undermining the ability of financial institutions to increase lending to the businesses of all sizes that want to invest and fuel our recovery. Our overriding goal in restructuring our financial architecture should be that taxpayers never again have to save a failing financial institution.

The debate recently has centered on big banks and trading risks. I agree that big banks do pose a dangerously large risk to our financial system, and I am troubled that concentration in the industry has only increased since the crisis. But if we are to protect our system from falling into trouble again, we need broad-based reform that covers all types of financial institutions and all forms of potentially risky activities.

For example, the most recent proposal by the Obama administration — to bar big banks from trading driven by other than customer-related activity — would not have prevented the collapse of Fannie Mae, Freddie Mac, Lehman Brothers, American International Group, Washington Mutual, Wachovia or other institutions whose failure contributed to the crisis. Rather than dictating a set of rules that will become out of date as the markets evolve, policy makers should devise legislation that ensures that regulators have the authority to tackle the issue of size and all potential systemic risks.

This calls for two vital changes. First, we must create a systemic risk regulator to monitor the stability of the markets and to restrain or end any activity at any financial firm that threatens the broader market. Second, the government must have resolution authority to impose an orderly liquidation on any failing financial institution to minimize its impact on the rest of the system.

Together, these two reforms will enable the regulatory system to better prevent the kinds of excesses that fueled our recent crisis, restore market discipline and keep the failure of a large institution from bringing down the rest of the system.

A single agency responsible for systemic risk would be accountable in a way that no regulator was in the run-up to the 2008 crisis. With access to all necessary information to monitor the markets, this regulator would have a better chance of identifying and limiting the impact of future speculative bubbles.

Given our global markets, we have to address the issue of size on a multinational level. We should work through the Financial Stability Board, a global regulatory agency with headquarters in Switzerland, to establish an international agreement calling for stronger capital and liquidity requirements for large, complex institutions. The need for adequate liquidity cushions is not as well understood, but in my judgment it is even more important than the need for banks to maintain higher capital levels.

As for our domestic approach, we now have different government regulators focusing on the individual trees, and we need one regulator accountable for looking at the entire forest. My preference is for the Federal Reserve to be the systemic risk regulator, because the responsibility for identifying and limiting potential problems is a natural complement to its role in monetary policy.

Congress, however, seems to be moving toward having a council of regulators perform this function. While that is not my preference, I believe a council can be workable if it is led by either the Treasury secretary or the Fed chairman, and is structured to ensure that strong decisions are reached quickly in a crisis. Too many such panels in government act by consensus, allowing a single member to render the council immobile.

No systemic risk regulator, no matter how powerful, can be relied on to see everything and prevent future problems. That's why our regulatory system must reinforce the responsibility of lenders, investors, borrowers and all market participants to analyze risk and make informed decisions. This is possible only if everyone understands that no financial institution is too big to fail, and that its investors and creditors will have to bear the consequences if it does.

To address the moral hazard issue, the government needs broad-based authority to liquidate any failing financial institution without going through the bankruptcy process, which is not well-suited for such complex firms in the midst of a financial crisis. We must send a clear signal to market participants that whenever this process is put in motion, the outcome is liquidation; we cannot leave any hope that we would inject taxpayer dollars to preserve the failing firm in its present form.

Winding down a large institution is difficult and time-consuming. The regulators with this responsibility will need to be trained to do the job. And we must also require all large firms to develop a road map for their liquidation well ahead of any failure.These are not the only necessary reforms — we must also address regulation of derivatives and our over-reliance on credit ratings agencies. Over time, we have to simplify the patchwork quilt of regulatory agencies and improve transparency so that consumers and investors can punish excesses through their own informed investing decisions. We have to examine the many policies that favor homeownership, and recalibrate our support for them. We must also tackle what is by far our greatest economic challenge — the reduction of budget deficits — a big part of which will involve reforming our major entitlement programs: Medicare, Medicaid and Social Security.

It has been a difficult, and humbling, two years for our nation. But every other major country has more significant economic problems than we do and, with the resilience of our economy and the ingenuity of our people, we can meet our challenges. Nonetheless, we must not lose our sense of urgency, or the political courage to make the necessary reforms to ensure our long-term prosperity.

Henry M. Paulson Jr., the secretary of the Treasury from 2006 to 2009, is the author of "On the Brink: Inside the Race to Stop the Collapse of the Global Financial System."

ONE HUNDRED ELEVENTH CONGRESS

Congress of the United States

House of Representatives

COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM

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HEARING NOTICE

April 7, 2010

To: **Domestic Policy Subcommittee Members**

From: **Majority Staff**

Subject: **Domestic Policy Subcommittee Hearing**

On **Wednesday, April 14, 2010 at 10:00 a.m., in Room 2154 of the Rayburn House Office Building**, the **Domestic Policy Subcommittee of the Oversight and Government Reform Committee** will hold a hearing entitled, **"ONDCP's Fiscal Year 2011 National Drug Control Budget: Are We Still Funding a War on Drugs?"**

The purpose of the hearing is to evaluate: (1) the priorities and objectives of the Office of National Drug Control Policy ("ONDCP") under the Obama Administration and how those goals are reflected in the 2011 Fiscal Year National Drug Control Budget ("Budget"); (2) whether the Administration's funding requests reflect a balanced and evidence-based approach to national drug policy; and (3) ONDCP's budget formulation and budget scoring process, including ONDCP's compliance with the budgetary reporting requirements of the ONDCP Reauthorization Act of 2006.

For further information concerning this hearing, please contact ***Claire Coleman, Counsel***, at ***(202) 226-5299.***

FEDERAL RESERVE BANK *of* NEW YORK
33 LIBERTY STREET, NEW YORK, NY 10045-0001

THOMAS C. BAXTER, JR.
GENERAL COUNSEL AND
EXECUTIVE VICE PRESIDENT

March 31, 2010

Mr. Edolphus Towns
Chairman
Committee on Oversight and Government Reform
United States House of Representatives
2157 Rayburn House Office Building
Washington, DC 20515-6143

Dear Chairman Towns:

Enclosed are my responses to the written questions I received following the January 27, 2010 hearing before the Committee on Oversight and Government Reform entitled, "The Federal Bailout of AIG." As you requested, an electronic version has been forwarded to the Chief Clerk of the Committee.

Please let me know if I can be of further assistance.

Respectfully yours,

Thomas C. Baxter, Jr.
General Counsel And
Executive Vice President

Enclosure

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<u>**Questions from Representative Marcy Kaptur**</u>

1. **In a memo obtained by the Committee from Sarah Dahlgren to you, she recommends the hiring of BlackRock Solutions to perform services for the Federal Reserve Bank of New York related to the Maiden Lane Facilities two and three. Can you tell me what Sarah Dahlgren's role was in regard to AIG?**

Starting in September 2008, and continuing to this day, Sarah Dahlgren has been the Head of the AIG Relationship Monitoring Team.

2. **Did you approve Ms. Dahlgren's request?**

Senior management of the Federal Reserve Bank of New York (the "FRBNY" or the "New York Fed") made the decision to hire BlackRock. As a member of senior management, I supported the recommendation.

3. **To whom at the New York Fed did BlackRock report? What level of oversight does the FRBNY have over BlackRock in its management of the three Maiden Lane facilities? Identify and provide all related documents.**

With respect to the establishment of Maiden Lane LLC ("ML"), BlackRock reported to Helen Mucciolo, a senior vice president at the New York Fed. With respect to the establishment of Maiden Lane II LLC ("ML II") and Maiden Lane III LLC ("ML III"), BlackRock reported to Sarah Dahlgren. Ongoing oversight of BlackRock relating to all three facilities is managed by the New York Fed's Investment Support Office, which is headed by Ms. Mucciolo. The Investment Support Office subjects BlackRock to a vendor management program, which includes, but is not limited to, annual attestations, on-site reviews, and reviews of SAS 70s.

4. **The Committee also obtained slides where BlackRock complete an analysis of the Maiden Lane III that some counterparties were in a place to experience losses, especially if there was a downturn. Did BlackRock share this information with the Federal Reserve Bank of New York, and if so, was this information used strategically in the negotiations around the counterparty payments? Identify and provide all related documents.**

Unfortunately, I am not in a position to address whether BlackRock may or may not have provided certain documents to the Committee but not to the FRBNY, for the simple reason that the FRBNY would not have received those documents. My staff and I would be happy to look at any documents that the Committee could provide in this respect.

The FRBNY requested and received analysis from BlackRock regarding the collateralized debt obligations ("CDOs") that ML III would eventually purchase, including such information as counterparty exposure, collateral composition (e.g., sector, ratings, vintage), CDO value implied from collateral already posted, and analysis of how the CDOs would perform under various economic scenarios. Such analysis can be found at FRBNY-TOWNS-R1-159958 – 160018, FRBNY-TOWNS-R1-204486 – 204545, FRBNY-TOWNS-R1-160567 – 160627,

FRBNY-TOWNS-R1-212037 – 212041, FRBNY-TOWNS-R1-143191 – 143203, and FRBNY-TOWNS-R1-180054 of the materials that the FRBNY submitted in anticipation of the hearing on January 27, 2010. This analysis is also contained within information packets that were prepared by BlackRock in advance of our negotiations with counterparties. These packets provided background on the CDOs and therefore helped to inform us before we commenced negotiations with the counterparties. These packets can be found at FRBNY-TOWNS-R1-147270 – 147313 of the materials that the FRBNY submitted in anticipation of the January 27, 2010 hearing.

5. How involved was BlackRock in the counterparty negotiations? Identify and provide all related documents.

BlackRock's role was to provide services to the New York Fed, including, for example, the analysis described above. To my knowledge, BlackRock was not directly involved in the counterparty negotiations.

6. Who at BlackRock did the NYFRB work with the most in regard all three Maiden Lane facilities?

In establishing the Maiden Lane facilities the New York Fed worked most closely with Roland Villacorta, Mark Wiedman, and Richard Prager.

7. How much profit is BlackRock expected to make managing the three Maiden Lane facilities?

While I do not know how much profit BlackRock is expected to make, we have made public the terms of the Maiden Lane facilities contracts with BlackRock, including the fee schedules setting forth the fees to which BlackRock is entitled. These Investment Management Agreements ("IMAs") can be found at http://www.newyorkfed.org/aboutthefed/Blackrock_ML.pdf. In addition, our Chief Ethics and Compliance Officer determined that the fee to be paid to BlackRock pursuant to our agreement was commercially reasonable.

8. What are you currently doing to test the firewalls put in place by BlackRock to prevent BlackRock Solutions from sharing its information with the rest of BlackRock? Did you just go on BlackRock's word or did you hire an outside entity to test the firewall – and if an entity did test this, did the firewall hold or not? Identify and provide all related documents. What do you do on a regular basis to ensure that BlackRock is not taking advantage of their management of the Maiden Lane facilities and their investment business?

The FRBNY and BlackRock entered into the three IMAs relating to the Maiden Lane facilities between September 9, 2008 and December 12, 2008. Each IMA contains guidance and describes requirements for BlackRock's handling of confidential information and conflicts of interest related to the Maiden Lane facilities. The IMAs also provide the FRBNY with the right to conduct reviews of BlackRock's compliance with the IMA requirements. As mentioned above, these IMAs can be found at http://www.newyorkfed.org/aboutthefed/Blackrock_ML.pdf.

The FRBNY engaged KPMG to conduct a review of BlackRock's compliance oversight of the Maiden Lane facilities. This review was conducted in November 2009 and included, among other things, an inspection of BlackRock's compliance policies and procedures, a risk-based assessment of BlackRock's compliance control environment and testing of certain controls to help assess the veracity of test work performed by BlackRock. We expect to receive KPMG's final report soon, and the FRBNY plans to continue conducting further periodic reviews of BlackRock's compliance with the IMAs for the duration of the New York Fed's relationship with BlackRock.

9. When was the first Goldman Sachs collateral call on its CDS with AIG? What prompted this call? How soon after Goldman's collateral call did other banks start making collateral calls? How many collateral calls, for what amount and from which banks rolled in on these CDS's in 2008? Why were all of the banks allowed to keep the monies received from the collateral calls on these CDS contracts in addition to the money paid to tear up the contracts?

Some of the collateral calls you mention took place before September 16, 2008, the day that the New York Fed agreed to lend up to $85 billion to AIG through a secured revolving credit facility. Before September 2008, the New York Fed did not have any dealings with AIG, so I respectfully submit that AIG would be in a better position to describe those collateral calls. For the collateral calls that took place between September 16, 2008 and December 31, 2008, I refer you to an AIG press release describing, among other things, the collateral posted to CDS counterparties after AIG received official assistance, which is available at: http://www.aig.com/aigweb/internet/en/files/CounterpartyAttachments031809_tcm385-155645.pdf.

As you note, the counterparties essentially received "par," with ML III purchasing the CDOs for their fair value and AIG obtaining the tear-up of the CDSs. As I mentioned in my testimony on January 27, there were essentially four reasons why this was done. First, there was little time, and substantial execution risk and attendant harm of not getting the deal done by the deadline of November 10th. AIG had attempted for some time to negotiate tear-ups of its CDS contracts with its counterparties under terms more favorable than Maiden Lane III, and it did not succeed. When the Federal Reserve contacted AIG's counterparties, we believed, based on AIG's own experience, that our probability of success of getting them to agree to concessions in a timely fashion was slim. Even in a best-case scenario, we did not expect that the counterparties would offer anything more than a modest discount to par. In our judgment, taking additional time to press further for a discount was not justified in light of the overwhelming risk and catastrophic consequences of failing to complete the transaction by November 10.

Second, the Federal Reserve had little or no bargaining power given the circumstances. This restructuring negotiation was taking place in November of 2008, less than two months after the decision to rescue AIG from insolvency and the infusion of tens of billions of dollars. The Federal Reserve had already acted to rescue AIG, and the counterparties fully expected that we would stand by that decision, especially because the economic situation had gotten worse, not better. So, the typical threat in such negotiations – we will stand down and watch AIG file for bankruptcy – would have been an idle threat had we made it. In addition, the counterparties were unwilling to offer concessions because their contractual rights were already well-protected. The value of the CDOs they held, combined with the $35 billion of collateral they had previously obtained from AIG was, in most cases, equal to or in excess of par value. Thus, if AIG defaulted, and even filed for bankruptcy protection, the counterparties would have kept both the collateral and the underlying CDOs (and would have been made whole if they had sold the CDOs for fair value).

Third, even if we had had bargaining power, the rating agencies were closely examining AIG for signs that it would not be able to address its financial situation. If they saw the Federal Reserve take any action that seemed to suggest a lack of full support, in particular a bankruptcy threat, it might well have led to an immediate downgrade and the irreversible destruction of AIG, with the attendant consequences on the financial stability of our economy.

Fourth, the CDS contracts that AIG entered with the counterparties afforded the counterparties the right to cash collateral. While these contracts turned out to be detrimental to AIG, they were beneficial from the perspective of the counterparties, and the counterparties expected their contractual rights would be respected.

10. What happened to the deals, including synthetic deals, that were in AIG's portfolio, getting significant collateral calls but did not go into Maiden Lane III? How much collateral has been posted against these deals, what is their current market value and what is the plan for them in the future?

Prior to the ML III transaction, the AIG-FP derivative transactions that experienced the most significant collateral calls were those involving "multi-sector" CDOs, where AIG sold protection on CDOs that were invested in a portfolio of residential or commercial exposures. Most of AIG-FP's multi-sector CDOs were resolved by ML III. Of those that were not, the vast majority involved what the market refers to as "synthetic" CDO transactions. As you may be aware, in synthetic CDOs, the underlying investments of the CDO are derivatives – generally, a portfolio of single-name CDS contracts referencing residential and commercial MBS – rather than a portfolio composed primarily of securities, as would be typical for a "cash" CDO.

As of March 25, 2010, AIG had a total of approximately $7.5 billion in notional exposure to multi-sector CDOs, of which the vast majority are synthetic CDO transactions. AIG has posted approximately $3.7 billion in collateral against its notional exposure to synthetic multi-sector CDOs. Consistent with AIG's objectives to wind down AIG-FP, the plan is to terminate the derivative transactions related to multi-sector CDOs over time in an orderly fashion in a manner that reduces the costs to the company and therefore preserves value to the taxpayer.

11. What is the legal analysis for why these deals were not transferred to ML III as it relates to their synthetic nature?

The FRBNY's lending to ML III was authorized by the Board of Governors of the Federal Reserve System (the "Board of Governors") under Section 13(3) of the Federal Reserve

Act. Section 13(3) permits Federal Reserve Banks to extend credit in "unusual and exigent circumstances" when authorized by the Board of Governors, but only insofar as such credit is "secured to the satisfaction" of the Federal Reserve Bank. In this transaction, the FRBNY extended credit to ML III to enable it to purchase certain assets from AIG-FP's counterparties. This loan was secured by a pledge over all of the assets of ML III. As such, the FRBNY was required to be secured to its satisfaction with the collateral that ML III was to acquire with the loan proceeds.

Legal staff from the Board and the FRBNY analyzed the nature of certain derivative contracts that AIG-FP had written with respect to securities of the type that are commonly referred to in the financial markets as synthetic CDOs and that were, at one point, proposed for inclusion in the structure. AIG-FP had written derivatives offering protection on what is sometimes referred to as the "unfunded" portion of certain synthetic CDOs, with the consequence that AIG-FP had the responsibility to provide funding if the synthetic CDO vehicle were required to make payment on the credit default swaps in which it was invested. We were not comfortable taking these synthetics as collateral for our loan to ML III.

12. What percentage of the deals transferred to ML III consisted of underlying synthetic bonds? Is there a threshold for which the Fed had drawn that would treat some as hybrid (meaning permissible for Maiden Lane III) and some as synthetic (presumably not)?

As described above, the New York Fed is required to be "secured to its satisfaction" in order to extend credit. The FRBNY was satisfied that the securities acquired by ML III constituted sufficient collateral for its lending. There were no CDOs that are sometimes referred to in the financial markets as "synthetic CDOs" or "hybrid synthetic CDOs" purchased by ML III.

There are certain CDOs in ML III that do have some synthetic mortgage-related securities as a portion of the CDO vehicle's investment portfolio. I understand that these synthetic securities are fully funded within the structure of the securities – that is, there is cash retained against the derivative payment obligations – such that the risk profile of these CDOs is similar to the cash CDOs contained in ML III and are therefore different from that which would be typical in either a "synthetic CDO" or a "hybrid synthetic CDO."

13. What investigations is the FRBNY doing into the managers of the bad deals that ML III owns? many real investors are suing bankers and deal issuers – does the Fed or Treasury have any plans to pursue similar lawsuits against the parties responsible for such bad deals?

While the FRBNY does not have actual knowledge of any bad deals in ML III, given the amount of RMBS held either directly by the Maiden Lane facilities or as collateral in the CDOs held in ML III, the FRBNY understands that there may be some "bad deals." As a result, the New York Fed has been investigating its options and ability, both individually and through emerging clearing houses, to pursue claims against issuers of securities held in the ML facilities where the pools of assets did not meet original eligibility criteria as set forth in the offering documents. In addition, the FRBNY has already successfully pursued situations where CDO managers had substantially ceased all management duties but sought to continue to earn fees.

14. Some of the owners of the CDOs purchase by Maiden Lane III were not the banks, but their clients. The banks keep their identities closely guarded, but they are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance?

The Federal Reserve executed the ML III transaction to stanch the liquidity drain on AIG, which threatened AIG's solvency. The failure of AIG in the fall of 2008 would have imposed significant financial losses on many individuals, households and businesses, shattered confidence in already damaged financial markets, and greatly increased fear and uncertainty about the viability of our financial institutions. The condition of individual counterparties, and their clients, was not a relevant factor to the design and execution of the transaction.

15. What analysis did they do of a rescue for the monoline insurers and why was this rejected? What communications were there with the NY insurance department and what assurances were provided as a result of these discussions? Were any strategies or data shared between the NYID and the OTS, the Fed or the Treasury? What communications and analysis were performed about the commutations executed by the monolines with counterparties such as Merrill, Calyon and Citibank?

As part of the Federal Reserve's mission to promote financial stability, the FRBNY has monitored the efforts by state insurance departments to restructure obligations of the monoline insurers, and has had the opportunity to confer with state insurance departments, such as the New York State Insurance Department, about these issues in the past. The FRBNY did not have conversations with the state insurance departments relating specifically to mechanisms for resolving AIG-FP's multi-sector CDO swap portfolio. Based on our monitoring efforts, it became readily apparent to us upon our arrival at AIG that the circumstances surrounding AIG-FP's derivative contracts on multi-sector CDOs were substantially different from those of the monoline insurers. In significant contrast to the derivative contracts written by monolines that I understand have proven somewhat more susceptible to commutation, the derivative contracts on multi-sector CDOs written by AIG-FP required the posting of substantial cash collateral. This represented an acute and immediate liquidity drain on the company as AIG was required to post collateral following a downgrade in its ratings, the ratings of the CDOs or a decline in the market value of the CDOs. Further, in contrast to AIG, the monolines were subject to state resolution statutes that created a well-established statutory resolution process to ensure an orderly unwind of a monoline's derivative exposures.

16. What is the explanation for the appearance of the CMBS deals in Maiden Lane III? how did AIG acquire this exposure? What is Project Max, as discussed in the BlackRock memo and what were the liquidity and funding mechanisms of these bonds while in AIG's portfolio? if AIG was in a net positive funding position, why were these bonds transferred to ML III and what was the impact on AIG's balance sheet – positive or negative? what

was the impact on Deutsche Bank's balance sheet? if negative for AIG and positive for DB, why were these deals including in ML III rather than kept at AIG?

AIG-FP sold protection on the super-senior tranche of CDOs that were backed mostly by residential MBS, but also sold protection to some extent on CDOs with exposure to commercial MBS. AIG-FP's derivative protection was provided through both CDSs and other types of credit derivative transactions. Project Max is a structure in which a commercial paper conduit issued asset-backed commercial paper ("ABCP") that was backed by super senior CDO securities which were, in turn, invested in commercial MBS. AIG-FP had agreed to purchase the ABCP if required by Deutsche Bank in certain circumstances. AIG effectuated this obligation by agreeing with Deutsche Bank to sell it protection on approximately $7.5 billion (as of November 10, 2008) of ABCP through a type of credit derivative called a total rate of return swap. In this credit derivative transaction, AIG agreed to pay for losses on the underlying ABCP, while at the same time earning the associated coupons on the ABCP of approximately 1-month Libor + 30 basis points and paying to Deutsche Bank a floating rate ranging from 1-month Libor + 18 basis points to 1-month Libor + 24 basis points. As the coupon on the ABCP exceeded the rate paid under the swap, the net funding position to AIG was positive.

Nevertheless, AIG specifically requested that this deal be resolved by ML III. Like other multi-sector CDO exposures, Project Max represented a significant source of liquidity pressure for AIG because the company was required to post collateral under the terms of the total rate of return swap if CMBS spreads (as measured by the CMBX index) widened, signaling deterioration in value of reference assets. Indeed, as of November 10, 2008, the company had posted approximately $5.6 billion in collateral. To the extent that the underlying ABCP defaulted and/or the CMBX further deteriorated, the company would have had to fund the remaining $2.2 billion. As such, the resolution of the transaction by ML III was beneficial to AIG, since it removed the current and potential collateral pressures and the risk that the ABCP could default. We do not know the effect on Deutsche Bank's balance sheet, because the effect would be determined by many other factors, and because the impact of the ML III transaction on counterparties like Deutsche Bank was not a relevant consideration to our execution of the transaction.

17. Some of the owners of the CDOs purchased by Maiden Lane III were not the banks, but their clients. They are almost certain not to be US institutional investors. Most of the CDOs bought by Maiden Lane III have been downgraded since their acquisition some severely. What was the rationale for the Fed ultimately providing liquidity to investors of no systemic importance? Who were the third party clients of Goldman (and others?) who benefited from the Maiden Lane III payments to Goldman? Was any investigation performed to determine who they were and whether they were appropriate recipients of taxpayer payments? Were any conflicts of interest investigated with respect to such payments?

As noted above, the Federal Reserve executed the ML III transaction because of the substantial risk that the failure of AIG in the fall of 2008 would impose significant financial losses on many individuals, households and businesses, shatter confidence in already fragile financial markets, and greatly increase fear and uncertainty about the viability of our financial institutions. The condition of the counterparties, and their clients, was not a relevant factor to the design and execution of the transaction.

18. What were the hiring criteria used for selecting BlackRock as the advisor for AIG and Maiden Lane III? What was the conflicts of interest policy? How was this checked against the transactions? Identify and provide all related documents.

BlackRock was selected for this assignment based on an assessment of its relevant expertise as an investment management firm with extensive experience in the market for mortgage-backed securities and collateralized debt obligations, and based on its ability to assemble a significant team with relevant expertise on very short notice. As a result of previous work performed for certain AIG subsidiaries, BlackRock already had extensive knowledge of the ML III assets, and it would have been exceedingly difficult, time-consuming, and costly for another investment manager to acquire the same level of knowledge. AIG was informed in advance of the FRBNY's potential engagement of BlackRock, and consented to the engagement by signing an appropriate conflicts waiver letter. That letter is included as Attachment 1.

19. In your testimony, you discuss conversations with the credit rating agencies over AIG in particular just before the loan to AIG and following. When was the very first time that the FRBNY started a conversation with any of the rating agencies? What was the nature of the conversation? How many times did the FRBNY speak to the credit rating agencies about AIG? How many times did the FRBNY speak to the credit rating agencies about any of the counterparties of AIG? Do you have any information that any of the counterparties of AIG contacted the credit rating agencies about AIG? From your perspective, how involved were the credit rating agencies in the plan to bailout AIG, create the Maiden Lane facilities and any other related activities connected to AIG or its counterparties? Identify and provide all related documents.

FRBNY staff, together with AIG, met with the credit rating agencies multiple times in the fall of 2008 to discuss and understand their assessment of AIG's current and future financial strength and prospects and to provide information regarding the U.S. government's initial and restructured support facilities. Meetings occurred with representatives of S&P, Moody's, Fitch, and AM Best. During these meetings, AIG, rating agency, and Federal Reserve officials discussed, among other things, AIG's level of leverage and debt servicing costs (including costs under the Federal Reserve's revolving credit facility), the losses and potential ongoing liquidity drains associated with AIG's securities lending program and CDSs on multi-sector CDOs, progress and expected progress in divesting assets and businesses, and the financial condition and business prospects of AIG's subsidiaries. AIG and Federal Reserve officials also described to the rating agency representatives the actions that the U.S. government proposed to take to restructure the assistance provided to AIG to further stabilize the company and provide the company time to restructure and wind down its operations in an orderly manner. Such actions included the injection of $40 billion in equity by the Treasury Department under the Troubled Assets Relief Program, the use of such proceeds to pay down an equivalent amount of borrowing under the Federal Reserve's revolving credit facility, establishment of the credit facilities for ML II and ML III, and the restructuring of the terms of the revolving credit facility to, among other things, reduce the maximum amount available from $85 billion to $60 billion. AIG, Federal

Reserve, and rating agency officials also discussed the potential impact of these and other factors on the credit ratings of the company and its subsidiaries. We have no information relating to contact between the counterparties of AIG and the credit rating agencies.

Questions from Ranking Member Issa

1. If an SEC filing by AIG on or after September 19, 2008, had violated the securities laws, should AIG have been able to avoid liability by demonstrating that all of its SEC filings were subject to review, editing, an approval by the FRBNY and its counsel? In March 2009, you suggested that AIG could avoid liability to its counterparties for revealing their identities because it was doing so at the FRBNY's direction: "If someone sues AIG, they can say the Fed told us to do it." Do you believe that this immunity would extend to AIG's securities filings, which were also being directed by the FRBNY? If not, why?

AIG at all times remained responsible for complying with its disclosure obligations under U.S. securities laws. During the period at issue, AIG devoted substantial resources to fulfilling its disclosure obligations, including obtaining expert legal advice from experienced outside law firms. The role of the FRBNY and its counsel was: (1) to work with AIG to further the goals of accuracy and consistency of AIG's filings with respect to transactions involving the FRBNY; and (2) to protect, where appropriate, the substantial taxpayer funds at stake. The FRBNY's involvement did not provide AIG any relief from its obligations under the securities laws. At the time of the e-mail you refer to, AIG and the Federal Reserve were taking steps to make public the identities of the counterparties in response to Congressional requirements. This led to the company expressing concerns about European bank secrecy laws. The quoted e-mail was one part of a discussion of how we could mitigate the company's concerns and still meet the requirements of Congress. My e-mail did not refer to U.S. securities laws.

2. On November 17, 2008, AIG submitted a draft SEC filing to the New York Fed and Davis Polk for review, edits, and approval. The filing reported that a new compensation package had been signed by AIG's CFO, David Herzog. Within 40 minutes, Marshall Huebner, the lead partner for Davis Polk's FRBNY business, sent an e-mail to you titled "READ ME." Huebner wrote, "Very bad timing to have this 8k come out just before the Secretary and the Chairman go before Waxman...Is there any chance – and maybe it is just too late – to get the Herzog comp package unagreed to?" AIG never filed the SEC filing, and evidently canceled Mr. Herzog's compensation package. What actions did you take as a result of Huebner's e-mail?

I contacted AIG to express my concerns regarding the proposed salary increase and bonus for their CFO. This compensation was never paid to Mr. Herzog. To his credit, Mr. Herzog had already indicated that he would decline this compensation package.

3. Did the cancellation of Mr. Herzog's compensation package, and the cancellation of AIG's intended SEC filing, serve any aim other than avoiding embarrassment "just before the Secretary and the Chairman go before Waxman"?

My objective in contacting AIG was to express my reservations about whether the magnitude of the proposed salary increase and bonus was an appropriate expenditure in light of the extraordinary assistance that the company had received. Our outside counsel shared these reservations, as is demonstrated by a fuller quotation from the cited email:

> "Very bad timing to have this 8k come out … right as the other TARPeys are announcing zero bonuses, and hopefully just before we actually get AIG to fundamentally redirect on retention and annual bonuses. Is there any chance – and maybe it is just too late – to get the Herzog comp package unagreed to?"

Further, Mr. Herzog himself concurred with the conclusion.

4. Do you believe that it is ever appropriate for the Fed, or Treasury, to force a public corporation that has received extraordinary federal financial assistance to make changes to its compensation arrangements, or take other actions, in order to avoid making disclosures under the securities laws? When are such actions appropriate?

The responsibilities for monitoring compensation at institutions that have received extraordinary federal financial assistance have been discussed at length in many forums. In all cases, the institutions remain responsible for meeting any resulting disclosure obligations.

5. Was it appropriate for the FRBNY to contact the SEC directly to argue that a portion of AIG's filings should be kept confidential and should not even be submitted to the SEC as part of its confidentiality determination? Or should the FRBNY have allowed AIG to conduct all communication with the SEC regarding its filings on its own?

As noted above, the role of the FRBNY and its counsel in reviewing AIG's disclosure was: (1) to work with AIG to further the goals of accuracy and consistency of AIG's filings with respect to transactions involving the FRBNY; and (2) to protect, where appropriate, the substantial taxpayer funds at stake. In the case of ML III, the potential risk to taxpayer funds resulting from the disclosure of commercially sensitive information was particularly acute. In that context, it was appropriate for the FRBNY to participate in discussions with AIG and the SEC regarding the confidentiality of information relating to ML III. In May 2009, the SEC agreed with AIG and the FRBNY that certain security-specific ML III information could remain confidential.

<u>Questions from Mr. Souder</u>

1. What is the purpose of an 8-K SEC filing and who bears the responsibility for AIG's financial disclosures with the SEC?

SEC-reporting companies are required to disclose specified events and issues through Form 8-K filings; Form 8-K can also be used for voluntary disclosures. As with all of its SEC filings, AIG bears the responsibility for the disclosures it makes on Form 8-K or otherwise.

2. What interest did the FRBNY have in AIG's SEC's filings?

The role of the FRBNY and its counsel in reviewing AIG's disclosures was: (1) to work with AIG to further the goals of accuracy and consistency of AIG's filings with respect to transactions involving the FRBNY; and (2) to protect, where appropriate, the substantial taxpayer funds at stake.

3. After September 19, 2008 AIG sent its SEC filings to the FRBNY's outside counsel, Davis Polk, for review and editing prior to submission. Is it appropriate for the FRBNY to be editing and reviewing AIG's financial disclosures?

It is appropriate and, in fact, customary for issuers to seek comments on their proposed disclosures from others involved in material transactions with the issuers. This reflects an effort to obtain input from multiple sources, and helps ensure the accuracy of the filings. The review by the FRBNY and its outside counsel was consistent with this standard market practice.

Questions from Ranking Members Bachus, Committee on Financial Services, participating by unanimous consent of the Committee

1. During the fall of 2008, were you aware of the offer by Goldman Sachs to tear up its CDS contracts with AIG, which would have saved taxpayers more than $5 billion? If so, why was this option not explored or acted upon?

To the best of my knowledge, no such offer was ever made. As Elias Habayeb, the former CFO of the Financial Services Division of AIG, wrote in his testimony before this committee, "In our ongoing discussions with counterparties during this period [the fall of 2008], the counterparties were unwilling to accept less than par value. Some counterparties were willing to terminate the swaps, but only if AIG purchased the underlying bonds from them – something AIG could not do without the NY Fed's help."

2. Have you been involved in any efforts to prevent disclosure of the New York Fed's assistance to AIG? Were you aware of the numerous emails from New York Fed official James Bergin that sought to gain special security status for AIG disclosures to the Securities and Exchange Commission – protections that are typically only used for national security purposes? Did you approve of these efforts? If not, who empowered Mr. Bergin with the authority to pursue obtaining possible national security status for AIG material from the SEC?

The role of the FRBNY and its counsel in reviewing AIG's disclosure was: (1) to work with AIG to further the goals of accuracy and consistency of AIG's filings with respect to transactions involving the FRBNY; and (2) to protect, where appropriate, the substantial taxpayer funds at stake. In the case of ML III, the potential risk to taxpayer funds resulting from the disclosure of commercially sensitive information was particularly acute. In that context, it was appropriate for the FRBNY to participate in discussions with AIG and the SEC regarding the confidentiality of information relating to ML III. Mr. Bergin, who is a lawyer working under my supervision, called the SEC, described the concern, and was offered a procedure that is ordinarily used in national security situations. He accepted the offer of this procedure to protect the taxpayer interest in AIG. In my view, this was a creative solution to a difficult problem, with the ultimate beneficiary being the American taxpayer. In May 2009, the SEC agreed with AIG and the FRBNY that certain security-specific Maiden Lane III information could remain confidential.

3. Were you aware of the January 13, 2009 email from Davis Polk & Wardwell attorney Diego Rotsztain that sought to ensure AIG's regulatory filings were kept secret and did "not get into the wrong hands?" Did you follow the advice of Mr. Rotsztain or approve of the efforts taken to conceal AIG's counterparty information?

When any reporting company makes a confidential treatment request ("CTR"), it is required to make a public filing that redacts the information subject to the request while simultaneously providing unredacted documents to the SEC office responsible for approving CTRs. I was aware that, because of the commercially sensitive nature of the information at issue and potential losses to the taxpayer from its disclosure, my legal colleagues took steps to help ensure that the information would not inadvertently become public during the CTR process. Among professionals, lawyers are especially sensitive to information that is privileged or confidential and are trained in how to protect it. In May 2009, the SEC agreed with AIG and the FRBNY that certain security-specific ML III information could remain confidential.

4. Were you aware of the December 4, 2008 email from New York Fed official Danielle Vincente which stated that releasing AIG's counterparty information would be "politically sensitive" and that "it would be hard to sell the public on US funds to buy foreign entities out of AIG risk, especially since the foreign regulators were contacted, etc.?" Other than demonstrating a full understanding that the decision to withhold information was political in nature, this email seems to imply that foreign regulators, such as France's Commission Bancaire, were willing to negotiate on AIG's counterparty payments to such institutions as Société Générale. Were these foreign regulators, in fact, willing to negotiate? If so, please provide a complete record of all Federal Reserve Bank of New York communications during these negotiations.

I was not aware of this particular e-mail until over a year after it was sent, and I do not believe that it accurately describes the rationale of the Federal Reserve's management regarding the issue of disclosure or the posture of the French authorities. While Ms. Vicente serves ably as a diligent staffer for the FRBNY, and we appreciate her many contributions, she did not participate in policy or management decisions concerning the counterparty negotiations or payments. The French authorities were not willing to negotiate.

5. Did you ever have any conversations with Secretary Geithner regarding the possible tear-up of Goldman's contracts with AIG? Was the lack of statutory authority for the New York Fed to act upon this possibility ever cited as a rationale for not accepting Goldman's willingness to tear up these contracts? Is so, who was responsible for citing this lack of authority?

I did not discuss this particular subject with then FRBNY President Geithner. As I mentioned in my answer to your first question, there was no willingness on the part of Goldman Sachs to tear up the swaps without receiving par on the underlying CDOs. And, as Mr. Habayeb testified, "[this was] something AIG could not do without the NY Fed's help." I have cited Section 4 of the Federal Reserve Act as authority for the proposition that the New York Fed must treat similarly situated financial institutions equally, and cannot discriminate among banks. Accordingly, I did not believe it was appropriate to treat French banks better than American banks when restructuring AIG's obligations to the counterparties.

6. During a January 26, 2009 interview with CNBC, Senator Jim Bunning claimed that the staff of the Federal Reserve was not in favor of rescuing AIG similar to the government's treatment of Lehman brothers. However, he cited an email from Chairman Bernanke to the Federal Reserve staff that served as a directive to save AIG due to the potential risk that AIG's failure might pose to the U.S. economy. Can you confirm or deny that this differing of opinion existed between the Fed's staff and Chairman Bernanke, and do you know if this e-mail does, in fact, exist?

Thousands of people work for the Federal Reserve, so I am sure that there were many different views on what should be done in response to the crisis at AIG. But I am not aware of any difference of opinion between Chairman Bernanke and senior staff at the Federal Reserve, nor do I have any personal knowledge of the e-mail cited by Senator Bunning.

Attachment 1

BLACKROCK
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October 28, 2008

Mr. Edward Liddy
Chief Executive Officer
American International Group, Inc.
70 Pine St
New York, NY 10005

Ms. Sarah Dahlgren
Senior Vice President
Federal Reserve Bank of New York
33 Liberty Street
New York, NY 10045

Dear Sir and Madam,

As you know, BlackRock Financial Management, Inc. is currently advising American International Group with respect to certain of the Financial Products Group portfolios and RMBS holdings (including the securities lending portfolio). At the request of the Federal Reserve Bank of New York (FRBNY), and as Ms. Dahlgren disclosed to Mr. Liddy on or about Monday, October 6, BlackRock is also advising the Federal Reserve Bank of New York with respect to the same AIG portfolios.

To date, the BlackRock team leaders serving AIG (namely, Zachary Buchwald and Nugzari Jakobishvilli) were not assigned to the FRBNY team. In this way, we have been able to ensure that information used in connection with the FRBNY engagement was not obtained as a result of the AIG engagement.

At this point, FRBNY has requested that the BlackRock-AIG team leaders mentioned above perform services for FRBNY and that information obtained in connection with the AIG engagement be shared with FRBNY.

Accordingly, we ask that AIG and FRBNY each execute a copy of this letter where indicated below to confirm that (1) it is aware that BlackRock is performing or has performed professional services for the other party, and that BlackRock will provide the services described above to FRBNY with respect to AIG; (2) it has had the opportunity to discuss the scope of such services with BlackRock; (3) it acknowledges and consents to BlackRock's performance of such services for each of them on their respective behalves; and (4) it will not make a claim against BlackRock based on an actual or perceived conflict of interest resulting from the circumstances described herein.

Please acknowledge your consent below.

40 East 52nd Street
New York, NY 10022
Tel 212.754.5300

BLACKROCK SOLUTIONS®

Yours sincerely,

Mark Wiedman
Managing Director

Acknowledged and agreed:

American International Group, Inc.

By: Edward M Liddy
Name: EDWARD M. LIDDY
Title: CHAIRMAN & CEO, AIG

Federal Reserve Bank of New York

By: Sarah Dahlgren
Name: Sarah Dahlgren
Title: Senior Vice President

40 East 52nd Street
New York, NY 10022
Tel 212.754.5300

March 31, 2010

BY FEDEX AND EMAIL

The Honorable Edolphus Towns, Chairman
Committee On Oversight and Government Reform
2157 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Towns:

I write in response to your February 22, 2010 letter enclosing questions from Representative Bachus following my appearance before the Committee on Oversight and Government Reform on January 27, 2010. Set forth below is my good faith attempt to respond to each of Representative Bachus's questions based on my personal knowledge and best recollection.

1. During the fall of 2008, were you aware of the offer by Goldman Sachs to tear up its CDS contracts with AIG, which would have saved taxpayers more than $5 billion? If so, why was this option not explored or acted upon?

AIG's early efforts to terminate the credit default swaps ("CDSs" or "swaps") written by AIG Financial Products ("FP") failed because AIG had no negotiating leverage with FP's counterparties to the swaps and AIG lacked the financial resources to effectuate any significant solution to its liquidity crisis without the assistance of Federal Reserve Bank of New York ("NY Fed"). After the federal rescue in September 2008, I was involved in discussions with Goldman Sachs about terminating certain of its swaps with FP, but no agreement was reached. Goldman's proposed prices were significantly below market value and would have resulted in additional losses to FP. After October 2008, the NY Fed took control of the negotiations with FP's counterparties, and I was not directly involved in any negotiations with counterparties, including with respect to the Maiden Lane III transaction. I am not aware of any offers from Goldman after the federal rescue, other than the offer described above.

Hon. Edolphus Towns
March 31, 2010
Page 2

2. Have you been involved in any efforts to prevent disclosure of the New York Fed's assistance to AIG? Were you aware of the numerous emails from New York Fed official James Bergin that sought to gain special security status for AIG disclosures to the Securities and Exchange Commission protections that are typically only used for national security purposes? Did you approve of these efforts? If not, who empowered Mr. Bergin with the authority to pursue obtaining possible national security status for AIG material from the SEC?

I, along with others, reviewed AIG's filings with the SEC to help ensure their accuracy because of my familiarity with the terms of the Maiden Lane III transactions. I did not decide what exhibits or schedules should be disclosed. AIG had inside and outside legal counsel who guided the Company through that process. I do not recall being aware of, nor would I have been consulted on, the procedures or protections afforded AIG's disclosures by the SEC.

3. Were you aware of the January 13, 2009 email from Davis Polk & Wardwell attorney Diego Rotsztain that sought to ensure AIG's regulatory filings were kept secret and did "not get into the wrong hands?" Did you follow the advice of Mr. Rotsztain or approve of the efforts taken to conceal AIG's counterparty information?

I was not aware of Mr. Rotsztain's email.

4. Were you aware of the December 4, 2008 email from New York Fed official Danielle Vicente which stated that releasing AIG's counterparty information would be "politically sensitive" and that "it would be hard to sell the public on US funds to buy foreign entities out of AIG risk, especially since the foreign regulators were contacted, etc.?" This email seems to imply that foreign regulators, such as France's Commission Bancaire, were willing to negotiate on AIG's counterparty payments to such institutions as Societe Generale. Were these foreign regulators, in fact, willing to negotiate? If so, please provide a complete record of all AIG communications during these negotiations.

I was not aware of Ms. Vicente's December 4, 2008 email and I was not aware of any discussions about the foreign regulators willingness to negotiate AIG's payments to counterparties at the time.

Hon. Edolphus Towns
March 31, 2010
Page 3

5. Did you ever have any conversations with Secretary Geithner regarding the possible tear-up of Goldman's contracts with AIG? Was the lack of statutory authority for the New York Fed to act upon this possibility ever cited as a rationale for not accepting Goldman's willingness to tear up these contracts? If so, who was responsible for citing this lack of statutory authority?

I have not had any conversations with Secretary Geithner regarding Goldman or on any other topic. I am not aware of any discussion about the NY Fed's authority to tear up Goldman's swaps with FP.

Sincerely,

Elias Habayeb

cc: The Honorable Darrell Issa, Ranking Minority Member
Committee on Oversight and Government Reform

Joseph S. Allerhand, Esq.

O

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March 10, 2010

BY HAND DELIVERY

The Honorable Edolphus Towns
Chairman, Committee on Oversight & Government Reform
United States House of Representatives
2157 Rayburn House Office Building
Washington, D.C. 20515-6143

Re: *Supplemental Questions for Stephen Friedman*

Dear Chairman Towns:

Please accept this letter in response to your letter of February 22, 2010 addressed to our client Stephen Friedman, which Mr. Friedman received on March 3, 2010. Your letter asked Mr. Friedman to provide written responses to several questions from Representative Spencer Bachus for inclusion in the hearing record relating to the public hearing before the Committee on Oversight and Government Reform ("Committee") on January 27, 2010, entitled "The Federal Bailout of AIG." Mr. Friedman appreciates the opportunity to respond to the Committee's questions and he has requested that we transmit the attached responses on his behalf.

Should you have any questions, please contact me at your earliest convenience.

Yours very truly,

Arthur B. Culvahouse, Jr.
of O'MELVENY & MYERS LLP

Enclosures

cc: The Honorable Darrell Issa
Ranking Member, Committee on Oversight and Government Reform
Stephen Friedman

Responses of Stephen Friedman to Supplemental Questions for the Record
from Rep. Spencer Bachus, Ranking Member, Committee on Financial Services

Committee on Oversight and Government Reform
Hearing on
"The Federal Bailout of AIG"
January 27, 2010

1. **During the fall of 2008, were you aware of the offer by Goldman Sachs to tear up its CDS contracts with AIG, which would have saved taxpayers more than $5 billion? If so, why was this option not explored or acted upon?**

As I noted in my prepared statement for the January 27, 2010 hearing, in my hearing testimony, and in the letters from my counsel to the Committee staff of January 15, 2010 and January 19, 2010, the structure and statutory framework of the Federal Reserve System gives the Board of Directors of the New York Federal Reserve Bank (the "Bank") no role in or authority over the regulation, supervision, or oversight of banks, bank holding companies, or other financial institutions. Rather, pursuant to the Federal Reserve Act, the Bank Directors' duties are limited to "mak[ing] recommendations on monetary policy" and supervising certain aspects of the Bank's administration, such as approving the Bank's budget, reviewing the Bank's internal controls and policies and procedures, and overseeing personnel matters, including assisting in the selection of the Bank President and other senior Bank officers. Any policy decisions relating to financial institutions are carried out by the officers of the New York Federal Reserve Bank, acting at the direction of the Board of Governors of the Federal Reserve System in Washington. During my service as a Director, the New York Federal Reserve Bank maintained robust policies and procedures to wall-off Directors from any decisions involving the regulation and supervision of banks, bank holding companies, or other financial institutions. As set forth in my statement and testimony, I and the other Directors of the New York Federal Reserve Bank were not involved in the decision to bail out AIG, the decision to repay the AIG counterparties at par, the decision not to publicly disclose those counterparties' names, or any other decisions related to the AIG rescue or AIG's regulatory disclosures. I did not ratify those decisions, I do not know who made those decisions, and I do not know why those decisions were made.

In response to Congressman Bachus's specific question, I do not recall having any knowledge in the fall of 2008 of an offer by Goldman Sachs to tear up its CDS contracts with AIG, whether in my capacity as a Director of the New York Federal Reserve Bank or in my capacity as a Director of Goldman Sachs. Directors of the Bank were neither involved in nor consulted in connection with negotiations with Goldman Sachs or other AIG counterparties. As I explained in my prepared statement, I received a summary courtesy briefing about the November 10, 2008 transaction to repay AIG's counterparties at par after the transaction had been completed, but this briefing did not include details about the Bank's negotiations with counterparties.

2. **Have you been involved in any efforts to prevent disclosure of the New York Fed's assistance to AIG? Were you aware of the numerous emails from New York Fed official James Bergin that sought to gain special security status for AIG disclosures to**

the Securities and Exchange Commission – protections that are typically only used for national security purposes? Did you approve of these efforts? If not, who empowered Mr. Bergin with the authority to pursue obtaining possible national security status for AIG material from the SEC?

No. I have not been involved in any efforts to prevent disclosure of the Bank's assistance to AIG, nor am I aware of the emails to which you refer. I did not approve or ratify these efforts. I do not know who empowered Mr. Bergin with the authority to pursue national security status for AIG material. Again, because Directors of the New York Federal Reserve Bank are walled-off from any decisions regarding individual financial institutions, any decisions related to the disclosure of the AIG counterparties' names were outside the scope of my authority as a Director of the Bank.

3. **Were you aware of the January 13, 2009 email from Davis Polk & Wardwell attorney Diego Rotsztain that sought to ensure AIG's regulatory filings were kept secret and did "not get into the wrong hands?" Did you follow the advice of Mr. Rotsztain or approve of the efforts taken to conceal AIG's counterparty information?**

No. I was not aware of the January 13, 2009 email from Mr. Rotsztain to which you refer. As explained above, any decisions related to the disclosure of AIG's counterparty information were outside the scope of my authority as a Director pursuant to the policies and procedures of the Bank. I therefore was not involved in and did not ratify or approve any decisions relating to AIG's regulatory filings or disclosure obligations.

4. **Were you aware of the December 4, 2008 email from New York Fed official Danielle Vicente which stated that releasing AIG's counterparty information would be "politically sensitive" and that "it would be hard to sell the public on US funds to buy foreign entities out of AIG risk, especially since the foreign regulators were contacted, etc.?" Other than demonstrating a full understanding that the decision to withhold information was political in nature, this email seems to imply that foreign regulators, such as France's Commission Bancaire, were willing to negotiate on AIG's counterparty payments to such institutions as Societe Generale. Were these foreign regulators, in fact, willing to negotiate? If so, please provide a complete record of all Federal Reserve Bank of New York communications during these negotiations.**

No. I was not aware of the December 4, 2008 email from Ms. Vicente to which you refer and I have no knowledge of whether foreign regulators were willing to negotiate on AIG's counterparty payments, other than what has been subsequently reported in the press.

5. **Did you ever have any conversations with Secretary Geithner regarding the possible tear-up of Goldman's contracts with AIG? Was the lack of statutory authority for the New York Fed to act upon this possibility ever cited as a rationale for not accepting Goldman's willingness to tear up these contracts? If so, who was responsible for citing this lack of statutory authority?**

No. As stated above, I was not aware of an offer by Goldman Sachs to tear up its CDS contracts. I did not have any conversations with Secretary Geithner regarding such an offer.

6. **During a January 26, 2009 interview with CNBC, Senator Jim Bunning claimed that the staff of the Federal Reserve was not in favor of rescuing AIG similar to the government's treatment of Lehman brothers. However, he cited an email from Chairman Bernanke to the Federal Reserve staff that served as a directive to save AIG due to the potential risk that AIG's failure might pose to the U.S. economy. Can you confirm or deny that this differing of opinion existed between the Fed's staff and Chairman Bernanke, and do you know if this email does, in fact, exist?**

No. I had no knowledge of whether there was a difference of opinion between the Federal Reserve staff and Chairman Bernanke on whether to rescue AIG prior to the January 27, 2010 hearing and I do not know whether the email you describe in fact exists. As I previously explained to the Committee, I did receive a summary courtesy briefing from senior Bank officers on the September 16, 2008 rescue of AIG after the decision to do so had been finalized, but that briefing did not include any information on internal Federal Reserve deliberations.

Responses of Stephen Friedman to Supplemental Questions for the Record
from Rep. Spencer Bachus, Ranking Member, Committee on Financial Services

Committee on Oversight and Government Reform
Hearing on
"The Federal Bailout of AIG"
January 27, 2010

1. **During the fall of 2008, were you aware of the offer by Goldman Sachs to tear up its CDS contracts with AIG, which would have saved taxpayers more than $5 billion? If so, why was this option not explored or acted upon?**

As I noted in my prepared statement for the January 27, 2010 hearing, in my hearing testimony, and in the letters from my counsel to the Committee staff of January 15, 2010 and January 19, 2010, the structure and statutory framework of the Federal Reserve System gives the Board of Directors of the New York Federal Reserve Bank (the "Bank") no role in or authority over the regulation, supervision, or oversight of banks, bank holding companies, or other financial institutions. Rather, pursuant to the Federal Reserve Act, the Bank Directors' duties are limited to "mak[ing] recommendations on monetary policy" and supervising certain aspects of the Bank's administration, such as approving the Bank's budget, reviewing the Bank's internal controls and policies and procedures, and overseeing personnel matters, including assisting in the selection of the Bank President and other senior Bank officers. Any policy decisions relating to financial institutions are carried out by the officers of the New York Federal Reserve Bank, acting at the direction of the Board of Governors of the Federal Reserve System in Washington. During my service as a Director, the New York Federal Reserve Bank maintained robust policies and procedures to wall-off Directors from any decisions involving the regulation and supervision of banks, bank holding companies, or other financial institutions. As set forth in my statement and testimony, I and the other Directors of the New York Federal Reserve Bank were not involved in the decision to bail out AIG, the decision to repay the AIG counterparties at par, the decision not to publicly disclose those counterparties' names, or any other decisions related to the AIG rescue or AIG's regulatory disclosures. I did not ratify those decisions, I do not know who made those decisions, and I do not know why those decisions were made.

In response to Congressman Bachus's specific question, I do not recall having any knowledge in the fall of 2008 of an offer by Goldman Sachs to tear up its CDS contracts with AIG, whether in my capacity as a Director of the New York Federal Reserve Bank or in my capacity as a Director of Goldman Sachs. Directors of the Bank were neither involved in nor consulted in connection with negotiations with Goldman Sachs or other AIG counterparties. As I explained in my prepared statement, I received a summary courtesy briefing about the November 10, 2008 transaction to repay AIG's counterparties at par after the transaction had been completed, but this briefing did not include details about the Bank's negotiations with counterparties.

2. **Have you been involved in any efforts to prevent disclosure of the New York Fed's assistance to AIG? Were you aware of the numerous emails from New York Fed official James Bergin that sought to gain special security status for AIG disclosures to the Securities and Exchange Commission – protections that are typically only used for**

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Exhibit Book

January 27, 2010 Hearing on "The Federal Bailout of AIG"

Committee on Oversight & Government Reform
U.S. House of Representatives

Exhibit Book Index

January 27, 2010 Hearing on "The Federal Bailout of AIG"

<u>Section</u>	<u>Subject</u>
1st Section	Treasury/Fed Involvement
2nd Section	Counterparty Negotiations
3rd Section	Systemic Justifications

Meeting notes

vincent.baldari

Steven.Manzari

10/02/2008 09:55 AM

Cc:

lawrence prybylski

Show Details

422

Steve, Attached are Hank's notes as requested, thanks.

Ernst & Young ®

New York Financial Services Office
Vincent Baldari Senior Manager Transaction Advisory Services

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423

DRAFT

Concrete Activities:

FRB Step in as Counterparty to Security Lending / Repurchase Agreements

- Immediately have FRB step in as counterparty to a Security Lending program with multiple AIG entities including Security Lending Pool of Insurance entities, AIG FP's unencumbered asset pool. Proceeds used to pay down outstanding FRB Credit Facility.
    - To dos:
        - Confirm eligibility of program for FRB
        - Determine which AIG entities have assets that would be eligible for the program
        - Assess eligibility of collateral for the FRB and haircuts
        - Determine funding level
        - Ensure that proceeds from any Security Lending program are used to pay down the Credit Facility
        - Determine Insurance regulatory angle related to the program
        - Replace AIG Investments as the Manager of the program
            - Develop criteria to liquidate assets in the pool as and where appropriate

Trade Guaranty for AIG FP (On hold)

- Provide Trade Guaranty to AIG FP counterparties (principally on Multi Sector CDOs) contingent upon counterparty agreeing to all three steps:
    - Returning collateral to AIG FP
    - Counterparty agreeing to release AIG Parent from guaranty in return for guaranty from FRB
    - Counterparty agreeing to remove termination triggers

  AIG FP uses proceeds of returned collateral to pay down FRB facility.

  - To dos:
    - Understand timing of this relative to MLII

Maiden Lane II and III

- Establish a entity(ies) to purchase RMBS, CMBS, Multi Sector CDOs and other FP derivatives (MLII and MLIII) from AIG FP, Security Lending program and other AIG entities. AIG would own and equity piece with a defined return and share in piece of the upside and FRB would provide financing (or guaranty a covered bond that would be financed with third party money). Security positions would be sold from AIG to MLII/III at current mark (subject to structural considerations). Financing would be needed to purchase securities and derivative settlements. Partial objective would be to sell RMBS from Security Lending program to clean up insurance balance sheets. Derivative positions would be sold at current marks (subject to structural considerations). All collateral posted to and from related to the derivative positions would be transferred. All trades under an existing CSA would be transferred (needs to be evaluated). A Liquidity facility would be needed to fund the physical settlement of CDS prior to liquidation of collateral. FRB would provide a keep well agreement/guaranty on the performance of all transactions within the structure.

Derivative Counterparty would need to agree to the following prior to novation:

- Transfer of all collateral to MLII/III
- Unwind of all prior FRB guarantees (if appropriate)
- Counterparty agreeing to release AIG Parent from guaranty in return for guaranty from FRB (or MLII/III)
- Counterparty agreeing to remove termination triggers
- Counterparty agreeing to novate trades to MLII/III.

Securities purchased would be available to settle contingent claims on derivatives. Cash collateral purchased from FP would be reinvested in liquid investments. Multi Sector component of entity would be similar in structure and activities to Athilon Capital. ML II/III would need a way to offset derivative positions that are transferred into book to mitigate market risks. May consider mirror trades with AIG FP or another street counterparty. MLII/III would hold credit risk on book for AIG FP and receive collateral on street derivatives.

Securities vs. derivatives could be split into two structures as needed.

To dos:

- Need to size the debt and equity (tranche activities)
- Determine pricing of liquidity facility, guarantee fee,
- Determine Risk management process, operational process
- Determine covered bond (third party) vs direct FRB lending.
- Open trading lines for replacing of book if not on a matched book basis
- Determine if CSAs can be split
- Assess what trades to circle and what trades to move – market risk management as key driver – determine assessment criteria
- Agent for risk management activities
- Legal agreements, due diligence…
- Determine what to do with Counterparties that do not want to move over (expected to be few)
- Determine mark process for moving trades between FP and ML II/III
- Assess hiring FP Treausury, Back Office … for trade operations (alternative party preferred) but timing unknown

Sarah Dahlgren/NY/FRS
10/04/2008 01:47 PM

To dan jester
cc
bcc
Subject attached presentation

was provided to us last night – we had asked AIG to pull together its plans for winding down AIG FP --- this was prepared by AIG, McKinsey and Blackrock.....the attached will be discussed with us on Monday.....it covers everything except the credit portions (for which they have supplied a different set of their own options (developed by Blackstone -- if you don't have those, I can have someone scan and send to you) and which we are proposing to deal with through the Maiden Lane 3 structure, although the firm doesn't know of our alternative yet).....

we can provide an update on Monday after discussions with the firm; the folks working on FP think that what the firm has laid out here is a reasonable plan, although execution may be difficult and the credit portion needs to be dealt with.....

AIG FP Restructuring Winddown Plan.pdf

* * * * * * * * * * * * * *
Sarah Dahlgren
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917-770-8147 (blackberry)

visit www.newyorkfed.org
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Calendar Entry
Meeting

Subject

Update on AIG Issues (Sarah Dahlgren)

When

Starts
Fri 10/10/2008
05:00 PM

Ends
Fri 10/10/2008
05:30 PM

30 mins

Invitees

Required (to)
Amy Flynn/NY/FRS@FRS, Clinton Lively/NY/FRS@FRS, dan.jester@do.treas.gov, James Hennessy/NY/FRS@FRS, Jim Mahoney/NY/FRS@FRS, Meg McConnell/NY/FRS@FRS, Paul Whynott/NY/FRS@FRS, Robert D Patalano/NY/FRS@FRS, Sandy Krieger/NY/FRS@FRS, Sarah Dahlgren/NY/FRS@FRS, Steven J Manzari/NY/FRS@FRS, Terrence Checki/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS

Optional (cc)
Deborah Kim/NY/FRS@FRS, Helen Ayala/NY/FRS@FRS, Helen Wendler/NY/FRS@FRS, Marlene Williams/NY/FRS@FRS, Rose Carofalo/NY/FRS@FRS, Suhayla Monroe/NY/FRS@FRS, Tanshel Pointer/NY/FRS@FRS

Chair

Timothy Geithner/NY/FRS

Sent By
Marlene Williams/NY/FRS

Where

Location
Mr. Geithner's Office

Number: 888-557-8511 code: 6799068#

Categorize

Description

#2
Conference bridge information:
Toll Free Dial in Number: 888-557-8511
Int'l Access/Caller Paid #: 215-446-3649
Access code: 6799068#

Agenda:
1. Rating agency strategy/issues
2. Maiden Lane II
3. Maiden Lane III

Your Notes

Sarah Dahlgren/NY/FRS
10/12/2008 07:49 PM

To dan jester
cc
bcc
Subject Fw: Update on AIG Issues (Sarah Dahlgren)

Dan -- just wanted to follow up with you on our meeting with Tim on Friday.....we agreed to move ahead on iterating with the rating agencies, starting first with Maiden Lane 2 (RMBS) ....we don't have approval yet to do it (and won't make any promises to the agencies). but we need to start getting them comfortable that there are solutions in the works to address the biggest issues at AIG.....we are starting with a session tomorrow moming with AIG folks to go over the RMBS solution (we've already previewed with Ed and a couple of his folks) and strategize for the set of meetings with the ratings agencies on Tuesday....

we'll plan to continue working out the details on Maiden Lane 3 over the beginning of the week, but won't show our cards to either AIG or the rating agencies until later in the week (and until after we've seen whatever progress can be made on tearing up trades at FP.....Larry Fink and Ed Liddy are coming in tomorrow to meet with Tim and me to talk about the tear-up process....)

we're also working through capital ideas as well as deal structure over the course of the week (with the hope of having a full package of things we can propose to do in the not-too-distant future).....

we'll keep you posted as the week continues.....if you have any thoughts/ideas or other things we should be thinking about. please give a holler.....

also, wanted to make sure you had the documents from Friday's call (ML 2 and rating agency strategy....ML 3 document will be sent around tomorrow)....

thanks....

Sarah

AIG FRBNY ML 2 10-10.ppt AIG Rating Agency Strategy.doc

* * * * * * * * * * * * * * *

Sarah Dahlgren
Senior Vice President
Federal Reserve Bank of New York
212-720-7537 (work)
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visit www.newyorkfed.org

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----- Forwarded by Sarah Dahlgren/NY/FRS on 10/12/2008 07:37 PM -----

Thomas Baxter/NY/FRS	To	Sarah Dahlgren/NY/FRS@FRS
10/15/2008 07:03 AM	cc	
	bcc	
	Subject	Re. AIG call tonight1529718FB1C008EE852576AF000F522A

Sarah,
This is progress, and I am sure you are the precipitating factor. There is real revisionist history here on ML 1 - it did not happen this way and I was there. We need to keep pushing, and I will try to do some today.

Sent from my BlackBerry Handheld.

----- Original Message -----
From: Sarah Dahlgren
Sent: 10/15/2008 12:56 AM EDT
To: Timothy Geithner; Thomas Baxter
Cc: Michael Silva; Meg McConnell; Michael Held; Kristin Mayer; Terrence Checki; Christine Cumming
Subject: Fw: AIG call tonight

To bring you up to speed following our discussions earlier this evening........we spent another hour with Board staff this evening on the way forward.....

1. We described the need for a broad set of solutions for the problem -- starting with the securities borrowing transaction last week; and indicated that it wasn't just one "fix" that was needed, but a package of things that addressed the key issues at the firm (liquidity and capital)....

2. We indicated that the programs announced this morning need to be assessed for applicability to AIG; Deborah Bailey confirmed that the FDIC wasn't looking to have AIG in the guarantee program longer than 30 days....she also indicated that it wasn't clear that it was the FDIC's call; we indicated that we were in discussions with the firm on their analysis and that we were doing the same -- but that additional clarity around all of them was needed, particularly since the agency press releases and other documents aren't all consistent across one another.....(also told them it didn't fix the problems, but possibly bought us some small amount of time)

3. We indicated that even with the programs announced this morning, we nevertheless needed to press forward on the set of solutions that we had in train -- namely, ML 2 and ML 3, deal restructuring and options on capital, and keepwell/guarantee options -- since it wasn't at all clear that any "bang" out of this morning's announcements would buy us anything other than a little time *Board staff again reiterated that they didn't think that the Governors (unnamed) would go for ML 2 or ML 3...their ears perked up, though, when we indicated that ML 2 would be done only as an "out" for the securities borrowing transaction and wouldn't be an "add" to the current total of programs (so, 24 in RMBS in exchange for 37.8 exited); they continue to push back hard on ML 3*

4. We described the rating agency process that we were intending to follow -- together with the firm -- starting tomorrow with Step 1 and leading up to announcement of 3Q earnings on November 5 (this can be accelerated if need be depending on rating agency reations, and any indications they are prepared to act):

Step 1: This week 10/13: two pieces to talk with the rating agencies about: a) discuss the Treasury/Fed/FDIC announcements in the context of AIG: new news, could have a positive impact, still needs to be assessed, work is being done to assess impact as well as garner more details on the options, etc.... and b) discuss the RMBS structure option, essentially on a no-name basis (so, the FRBNY's name isn't on any of the slides the firm will be using) to elicit feedback from the rating agencies on the "total sec lending solution".....

Step 2: Begining of next week 10/20: two pieces here as well: a) open discussions on FP possibilities -- essentially working through the ML 3 concepts and any other solutions that come through those discussions; and b) discussion on restructuring of loan terms (rate, ticking fee, maturity, etc....)

Step 3: End of next week 10/25: one piece: a) discussion of the capital options

Step 4: Beginning of 10/27: one piece: a) keepwell/guarantee *Board staff emphatically said this was off the table; we countered with questions about why it was so clearly off the table and suggested, as well, that perhaps this was something that Treasury could do.....they weren't willing to consider it -- and suggested that we needed to do some work with Treasury to get them to do the keepwell/guarantee ...we think this is something we need to have in our back pockets just for contingency purposes -- if a ratings downgrade happens at any time in the next three weeks or afterwards, we will need this to protect any value in the insurance companies and, importantly, to avoid a disorderly seizure by regulators of the insurance companies (we'll provide more details on this in our bankruptcy discussion)....*

Board staff agreed with our plan to move ahead with Step 1; they are reluctant to give any go ahead on Step 2 (particularly ML 3/Financial Products solutions) and seemed open to talking about deal structure and capital options.....*the rating agencies, though, are going to be looking for the FP solutions sooner rather than later (the second fix for the lother liquidity bleed in the company)*

we agreed to talk again later in the week (meanwhile, we are continuing to include them in all discussions on ML 2 and ML 3, as well as other briefing opportunities)

Rich and Kieran ended on a relatively positive note (I'm looking for any positives these days) by indicating that they are wiling to do what they can at Board staff; that there is a realization by the Governors that they may need to lend more to obviate the systemic risks and they aren't against lending more into a troubled situation if necessary to prevent systemic implications; finally, either Kieran or Rich indicated that the Governors have cited the Bear Stearns deal as a one-off deal that was done on the understanding it wouldn't be done again (so ML 2 and ML 3 aren't well-received...)....We asked again -- if they have other options that we should be putting on our list of things to consider, we're very open to that.....

We'll be coming back to you with our thinking on the restructuring of the deal and capital issues later in the week; we're making progress on that front even though we just started tonight, but should have something to share later in the week.....

Questions that were asked repeatedly by staff on the call (but were attributed to Governors):

1. What does any of this buy us?

2. What if the rating agencies still downgrade the firm? *(this is why they have to think much longer/harder onthe keepwell/guarantee question)*

3. What are the systemic implications of a downgrade? *(clearly this is still a "to do" for us as the Governors haven't gotten any more comfortable with answers thus far provided by Board staff; we are working on a presentation that we can walk through anyone who is interested; we agreed with Staff that we would aim to do a round with them at the beginning of next week and a round with the Governors right after that; Board staff is working with Clint to also provide input on the systemic implications of FP)*

4. Treasury has communicated that it is not interested in doing anything for AIG. What is your next step here? *(that was directed at the FRBNY)*

5. Aren't you using the leverage and influence that you have on the firm to be forcing them to use the money we are providing to them to FIX the problems? *(don't get me started on answering this one.....)*

Holler if you have questions or want to follow up more on any of these issues......

Sarah

* * * * * * * * * * * * * *
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visit www.newyorkfed.org
* * * * * * * * * * * * * *
----- Forwarded by Sarah Dahlgren/NY/FRS on 10/14/2008 11:47 PM -----

Rich Ashton/BOARD/FRS@BOARD
10/14/2008 07:27 PM

To
Sarah Dahlgren/NY/FRS@FRS
cc
Kieran Fallon/BOARD/FRS@BOARD, Jon D Greenlee/BOARD/FRS@BOARD, Michael S Gibson/BOARD/FRS@BOARD, Deborah P Bailey/BOARD/FRS@BOARD
Subject
AIG call tonight

Sarah, For our call tonight we wanted to update you on where we stand at the Board as of today. We have not gotten clearance on either of the Avon or Nova structures, and there may still be some legal obstacles with these proposals. We are especially concerned about the novation of the CDS portfolio, which still looks more like a guarantee, which we can't do, than a loan. So you still should not discuss these strategies tomorrow.

Moreover, there may be a more solid basis for the rating agencies to at least consider holding off issuing a new rating for AIG. As you know, the FDIC just announced yesterday the implementation of a guarantee program that will fully guarantee for 30 days the senior unsecured debt of eligible U.S. savings and loan holding companies. After 30 days, eligible institution will have the option to continue in the guarantee program in return for the payment of a guarantee fee. Obviously, if AIG qualifies for the FDIC guarantee program that fact should have a significant bearing on the company's debt ratings. Given that the guarantee program was just announced this morning, AIG and the rating agencies are probably still scrambling to figure out how the guarantee program may impact the company and its credit ratings. Until that gets sorted out more definitively, it would seem premature (and potentially irresponsible) for the rating agencies to go to committee on AIG's credit rating.

Thomas Baxter/NY/FRS
10/15/2008 07:03 AM

To: Sarah Dahlgren/NY/FRS@FRS
cc:
bcc:
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3. We indicated that even with the programs announced this morning, we nevertheless needed to press forward on the set of solutions that we had in train -- namely, ML 2 and ML 3, deal restructuring and options on capital, and keepwell/guarantee options -- since it wasn't at all clear that any "bang" out of this morning's announcements would buy us anything other than a little time *Board staff again reiterated that they didn't think that the Governors (unnamed) would go for ML 2 or ML 3...their ears perked up, though, when we indicated that ML 2 would be done only as an "out" for the securities borrowing transaction and wouldn't be an "add" to the current total of programs (so, 24 in RMBS in exchange for 37.8 exited); they continue to push back hard on ML 3*

4. We described the rating agency process that we were intending to follow -- together with the firm -- starting tomorrow with Step 1 and leading up to announcement of 3Q earnings on November 5 (this can be accelerated if need be depending on rating agency reations, and any indications they are prepared to act):

Step 1: This week 10/13: two pieces to talk with the rating agencies about: a) discuss the Treasury/Fed/FDIC announcements in the context of AIG: new news, could have a positive impact, still needs to be assessed, work is being done to assess impact as well as garner more details on the options, etc.... and b) discuss the RMBS structure option, essentially on a no-name basis (so, the FRBNY's name isn't on any of the slides the firm will be using) to elicit feedback from the rating agencies on the "total sec lending solution".....

Step 2: Begining of next week 10/20: two pieces here as well: a) open discussions on FP possibilities -- essentially working through the ML 3 concepts and any other solutions that come through those discussions; and b) discussion on restructuring of loan terms (rate, ticking fee, maturity, etc....)

Step 3: End of next week 10/25: one piece: a) discussion of the capital options

Step 4: Beginning of 10/27: one piece: a) keepwell/guarantee *Board staff emphatically said this was off the table; we countered with questions about why it was so clearly off the table and suggested, as well, that perhaps this was something that Treasury could do.....they weren't willing to consider it -- and suggested that we needed to do some work with Treasury to get them to do the keepwell/guarantee ...<u>we think this is something we need to have in our back pockets just for contingency purposes -- if a ratings downgrade happens at any time in the next three weeks or afterwards, we will need this to protect any value in the insurance companies and, importantly, to avoid a disorderly seizure by regulators of the insurance companies (we'll provide more details on this in our bankruptcy discussion)....</u>*

Board staff agreed with our plan to move ahead with Step 1; they are reluctant to give any go ahead on Step 2 (particularly ML 3/Financial Products solutions) and seemed open to talking about deal structure and capital options.....*the rating agencies, though, are going to be looking for the FP solutions sooner rather than later (the second fix for the lother liquidity bleed in the company)*

we agreed to talk again later in the week (meanwhile, we are continuing to include them in all discussions on ML 2 and ML 3, as well as other briefing opportunities)

Rich and Kieran ended on a relatively positive note (I'm looking for any positives these days) by indicating that they are wiling to do what they can at Board staff; that there is a realization by the Governors that they may need to lend more to obviate the systemic risks and they aren't against lending more into a troubled situation if necessary to prevent systemic implications; finally, either Kieran or Rich indicated that the Governors have cited the Bear Stearns deal as a one-off deal that was done on the understanding it wouldn't be done again (so ML 2 and ML 3 aren't well-received...)....We asked again -- if they have other options that we should be putting on our list of things to consider, we're very open to that.....

We'll be coming back to you with our thinking on the restructuring of the deal and capital issues later in the week; we're making progress on that front even though we just started tonight, but should have something to share later in the week....

Questions that were asked repeatedly by staff on the call (but were attributed to Governors):

1. What does any of this buy us?

2. What if the rating agencies still downgrade the firm? *(this is why they have to think much longer/harder onthe keepwell/guarantee question)*

3. What are the systemic implications of a downgrade? *(clearly this is still a "to do" for us as the Governors haven't gotten any more comfortable with answers thus far provided by Board staff; we are working on a presentation that we can walk through anyone who is interested; we agreed with Staff that we would aim to do a round with them at the beginning of next week and a round with the Governors right after that; Board staff is working with Clint to also provide input on the systemic implications of FP)*

4. Treasury has communicated that it is not interested in doing anything for AIG. What is your next step here? *(that was directed at the FRBNY)*

5. Aren't you using the leverage and influence that you have on the firm to be forcing them to use the money we are providing to them to FIX the problems? *(don't get me started on answering this one.....)*

Holler if you have questions or want to follow up more on any of these issues.... ..

Sarah

* * * * * * * * * * * * * *
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----- Forwarded by Sarah Dahlgren/NY/FRS on 10/14/2008 11:47 PM -----

Rich Ashton/BOARD/FRS@BOARD

10/14/2008 07:27 PM

To: Sarah Dahlgren/NY/FRS@FRS
cc: Kieran Fallon/BOARD/FRS@BOARD, Jon D Greenlee/BOARD/FRS@BOARD, Michael S Gibson/BOARD/FRS@BOARD, Deborah P Bailey/BOARD/FRS@BOARD
Subject: AIG call tonight

Sarah, For our call tonight we wanted to update you on where we stand at the Board as of today. We have not gotten clearance on either of the Avon or Nova structures, and there may still be some legal obstacles with these proposals. We are especially concerned about the novation of the CDS portfolio, which still looks more like a guarantee, which we can't do, than a loan. So you still should not discuss these strategies tomorrow.

Moreover, there may be a more solid basis for the rating agencies to at least consider holding off issuing a new rating for AIG. As you know, the FDIC just announced yesterday the implementation of a guarantee program that will fully guarantee for 30 days the senior unsecured debt of eligible U.S. savings and loan holding companies. After 30 days, eligible institution will have the option to continue in the guarantee program in return for the payment of a guarantee fee. Obviously, if AIG qualifies for the FDIC guarantee program that fact should have a significant bearing on the company's debt ratings. Given that the guarantee program was just announced this morning, AIG and the rating agencies are probably still scrambling to figure out how the guarantee program may impact the company and its credit ratings. Until that gets sorted out more definitively, it would seem premature (and potentially irresponsible) for the rating agencies to go to committee on AIG's credit rating.

Capital/Facility Strategy

Sarah Dahlgren

to:

Timothy Geithner, Thomas Baxter, Terrence Checki, christine.cumming, Sandy Krieger

10/19/2008 09:52 PM

Cc:

Michael Silva, Meg McConnell, Michael Held, Steven.Manzari, paul.whynott, Robert D Patalano, Jim Mahoney, james.hennessy

Show Details

We wanted to send along the deck that MS has developed and that we walked through this evening with them; we provided some feedback and want to see a couple of additional slides added (for example, we asked that they produce a companion slide to page 12 that would show a possible scenario given revised tenor of the facility, new asset values, current market environment, etc.... so that we could see what a modified divestiture and capital structure plan might look like; also, we've asked them to do some analysis on the current market environment and expectations looking out over time to assess the "value" of extending the asset dispositions over a longer period of time......) Both Kevin Warsh and Dan Jester have asked to see this as soon as possible (told them we'd have something tomorrow to share) -- but wanted to give you a chance to see it and ask questions before shooting it out to them.....if you'd like to talk tomorrow about this, let us know.....we're also working with E&Y to figure out changes on the terms of the loan (like 0% vs. 1.75%, no commitment fee, tenor, etc...) and impact of those changes (which the rating agencies don't seem too interested in -- they're basically ignoring the PIK for now since it doesn't have cashflow implications...and haven't really factored it into the amount we'd be owed back in two years either....although they'd like to see the company have more time to dispose of assets) * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * * *

- AIG 2008.10.19 Capital Structure v2.pdf

Sarah Dahlgren/NY/FRS
10/20/2008 09:24 PM

To Kevin Warsh/BOARD/FRS, dan jester
cc Timothy Geithner/NY/FRS@FRS
bcc
Subject Draft Capital Proposal

As we discussed -- we worked with Morgan Stanley over the weekend to develop some options on capital/facility structures that would address the rating agency concerns and provide the company with some flexibility in the near-term to address problems and dispose of assets....the capital/facility recommendations would be in addition to Maiden Lane 2 (RMBS solution) and Maiden Lane 3 (CDS solution) solutions......

The attached is still a work-in-progress; we have a couple more scenarios/ideas that we've asked them to go through (including other options on capital raising, etc...), as well as legal analysis of options that we still need to complete; we expect to have a full package of solutions to discuss mid-week (in anticipation of further iterations with rating agencies this week and next)......

Please holler if you have questions or other feedback we should be considering.....thanks!

AIG 2008.10.20 Capital Structure v6.pdf

* * * * * * * * * * * * * *
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Sarah Dahlgren/NY/FRS
10/20/2008 10:39 PM

To Thomas Baxter/NY/FRS@FRS, Timothy Geithner/NY/FRS@FRS, Terrence Checki/NY/FRS@FRS
cc
bcc
Subject Fw: Need to talk

History: This message has been replied to.

I think the "support your efforts" part of this message sounds positive.....and, in fact, I just got off the phone with Greenlee ....so, they really are serious about helping and the effort that Warsh/Kohn want to push is the "overall solution" to take to Treasury (something along the lines of ML 2 and ML 3, plus restructuring of the facility PLUS a slug of capital from Treasury)...Jon mentioned that they would like to see how to use TARP money to fix the capital structure of the firm and to hold off the rating agencies for a good amount of time (so, don't do bandaids).....as for the capital purchase plan limitations, with AIG's RWA, they'd be eligible for around $15B at 3% of RWA (maybe a little less....and we still have to deal with the OTS).....

on the guarantee front, assuming that the eligibility criteria will be consistent with the capital program and AIG qualifies, there may actually be room for additional capacity under this program if the answer to the question in the FAQs: "For an eligibile entity that had little or no senior unsecrued debt on September 30th, how will you determine how much you will guarantee?" can be interpreted positively for the AIG case: <u>"These entities will able to issue debt under the program and the amount will be determined by the FDIC on a case-by-case basis in consultation with the eligible entity's primary federal regulator...."</u> and since the guarantee can also be used on the CP facility -- let's get that 75 bp guarantee on anything that AIG puts in the CPFF.....(okay, perhaps this is greedy.....can we really get the CP guaranteed and get, say, $10B of senior guaranteed debt?.....).....

so, in fact, we could come up with several options that include all possibilities: the additional capital from Treasury and a slug of guaranteed senior debt from the FDIC and the guarantee on the CP....and then whatever we do to fix the facility......it's like a three-way pain sharing agreement.....

We're setting up a call to discuss further with Board staff tomorrow -- we'll walk through an updated version of the MS capital/facility structure (I've attached tonight's version...modest changes from yesterday's version......there's more work still to be done on the other equity raising options (as well as TARP and the guarantee program), as well legal analysis) -- to get their input/make them comfortable....

Further, Jon was very clear that they didn't want to get in our way and were really trying to be helpful.....he was apologetic in fact....and assured me they didn't want to interfere (third time he used the word).......

so, for some strange reason, this evening looks like it's all about POSSIBILITIES......

* * * * * * * * * * * * * *
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* * * * * * * * * * * * * *
----- Forwarded by Sarah Dahlgren/NY/FRS on 10/20/2008 09:26 PM -----

Jon.D.Greenlee@frb.gov
10/20/2008 07:07 PM

To "Sarah Dahlgren" <Sarah.Dahlgren@ny.frb.org>
cc
Subject Need to talk

Some of us spoke with Kohn and Warsh today about the situation and they gave us some thoughts and direction for us to support your efforts. I can send you an email later but it may be better talk and plan to set up a call some time tomorrow for the group.

Jon

Sent from my BlackBerry Wireless Handheld

Sarah Dahlgren/NY/FRS
10/21/2008 11:25 AM

To: Kevin Warsh/BOARD/FRS@BOARD
cc:
bcc:
Subject: Re: Draft Capital Proposal0883BCFB935782D5852576AF0011A86E

thanks -- I talked with Jon Greenlee last night and we are having a call at 3:00 with staff to go through a revised version of the MS presentation (that includes more of the things that we talked about last night...with some numbers on the impact of the preferred. etc....)....we're planning to send down another version, but if you want to shoot this one around in the interim, that's fine.....

will keep you posted...thanks for your help!

* * * * * * * * * * * * * *
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Kevin Warsh/BOARD/FRS@BOARD
10/21/2008 09:52 AM

To: Sarah Dahlgren/NY/FRS@FRS
cc:
Subject: Re: Draft Capital Proposal

thanks sarah. don and i met with Board staff yesterday and had call with tim along these lines.

does Board staff have draft MS presentation? ok if i forward?

thx

Sarah Dahlgren/NY/FRS@FRS
10/20/2008 09:21 PM

To: Kevin Warsh/BOARD/FRS@BOARD, dan.jester@do.treas.gov
cc: Timothy Geithner/NY/FRS@FRS
Subject: Draft Capital Proposal

As we discussed -- we worked with Morgan Stanley over the weekend to develop some options on capital/facility structures that would address the rating agency concerns and provide the company with some flexibility in the near-term to address problems and dispose of assets....the capital/facility recommendations would be in addition to Maiden Lane 2 (RMBS solution) and Maiden Lane 3 (CDS solution) solutions......

The attached is still a work-in-progress; we have a couple more scenarios/ideas that we've asked them to go through (including other options on capital raising, etc...), as well as legal analysis of options that we still need to complete; we expect to have a full package of solutions to discuss mid-week (in anticipation of further iterations with rating agencies this week and next)......

Please holler if you have questions or other feedback we should be considering.....thanks!

AIG 2008.10.20 Capital Structure v6.pdf

* * * * * * * * * * * * * *

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Sarah Dahlgren/NY/FRS
10/23/2008 07:55 AM

To: Timothy Geithner/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS
cc:
bcc:
Subject: Board staff

we briefed them last night:

Maiden Lane 2: Scott has reservations; but the legal issues aren't as sticky as thye could be; Rich Ashton thinks they are making progress on this

Maiden Lane 3: the new structure (buying in CDOs) is much better and easier to analyze than the CDS structure; they like this one; probably has sticky legal issues as above, but they didn't think it would be problematic

Krozner said Treasury couldn't do keepwells/guarantees....

and they were going to talk with Kevin/Don about how to convert out debt to preferred (beyond we didn't have the legal authority).....

* * * * * * * * * * * * * * *

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Fw: follow-up from calls today

Sarah Dahlgren

t
o
:

Steven.Manzari

10/24/2008 08:08 AM

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442

* * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * * * ----- Forwarded by Sarah Dahlgren/NY/FRS on 10/24/2008 08:03 AM -----

Meg McConnell/NY/FRS

10/24/2008 12:16 AM

To
Sarah Dahlgren/NY/FRS@FRS, Timothy Geithner/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS, Terrence Checki/NY/FRS@FI
cc

Subject
Re: follow-up from calls todayLink

One reaction to this request: Is the "recovery value to FRBNY" the right metric by which to gauge these alternative options? In other words, suppose we find that our expected recovery value is highest under option 1? Does this mean we should choose option 1? If not, what is a better way to rank these alternatives? My preference would be to model the relative present values of the tax payer losses across the range of scenarios you laid out in your slide deck, and to choose the scenario that minimizes those losses. The results of this exercise, which may or may not be consistent with maximizing the recovery value to FRBNY on our outstanding facility, would give us insight into how to best achieve our original objective of avoiding a systemic default (at least that is what I'd understood our objective to be...if instead we got into this for the purpose of making as much as possible or losing as little as possible for FRBNY on AIG, then I like Dan's suggestion). And if we find that minimizing the taxpayer losses requires an equity injection, then Treasury should probably get cracking on that soon, as the Fed doesn't have the authority to do it and we're all quickly running out of time. Margaret M. McConnell Federal Reserve Bank of New York 212-720-8773 ----- Original Message -----

From: Sarah Dahlgren **Sent:** 10/23/2008 10:32 PM EDT **To:** Timothy Geithner; Thomas Baxter; Terrence Checki; Meg McConnell **Subject:** follow-up from calls today fyi.....after our discussions this afternoon, Dan Jester called Pete Juhas to ask him to run a couple of analyses for him for discussions tomorrow.....essentially asking for the relative recovery by the FRBNY under three scenarios:1. Do nothing option (our option #1) 2. Do ML 2 and ML 3, lengthen maturity and reduce rate (our option #2)3. Subordinate $40B and do everything else (essentially our #7 option)Pete will pull this together tonight and we're going to talk with the MS team at 7:30 a.m. before he forwards the information to Dan; as well, he's going to include two sets of analyses -- one with the $85B looking at the 3 scenarios and one that represents a stress scenario of $100B..... Kevin also called Pete (after Dan called Pete) -- Pete described what Dan had asked for and the approach we were going to take .....we'll send around the analysis in the morning.... let me know if you want to see it before it is sent on in the morning ..... * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * * *

443

Re: Update on Dan Jester Call

Marc.Symons

to:

Sarah.Dahlgren

10/25/2008 06:06 PM

Cc:

chris.mcshea, "Bischof, Eric (IBD)", "Juhas, Peter (IBD)", Steven.Manzari, vincent.baldari

Show Details

444

Peter - here is the forecast for Q3 as of 10/23 - still a loss of $17 billion - this is the last forecast we have - let us know if you need anything else. Thanks, Marc

Marc C. Symons | Partner | Transaction Advisory Services - Financial Services Industry

Ernst & Young LLP

5 Times Square, New York, NY 10036, United States of America

Office: +1- 212- 773-0796 | Fax: +1- 866-786-3616 | Marc.Symons@ey.com

Mobile: +1-917-439-3699 EY/Comm: 9367966

Assistant: Emily Villatoro | Phone: +1- 212-773-0963 | Emily.Villatoro@ey.com

Sarah.Dahlgren@ny.frb.org

10/25/2008 05:51 PM

To

"Juhas, Peter (IBD)" <Peter.Juhas@morganstanley.com>

cc

amy.flynn@ny.frb.org, "Angelova-Makki, Anna (IBD)" <Anna.Angelova-Makki@morganstanley.com>, "Bischof, Eric (
<Kevin.J.Ryan@morganstanley.com>, "Singh, Shelley (IBD)" <Shelley.Singh@morganstanley.com>, ethan.james@dpw
diego.rotsztain@dpw.com, Marc.Symons@ey.com, chris.meshea@ey.com, marshall.huebner@dpw.com, Jim Mahoney@
Alejandro.LaTorre@ny.frb.org

Subject

Re: Update on Dan Jester Call

Thanks Peter ..... sounds like the materials for a TARP meeting could be built into the "ultimate" background/justification deck for this solution set..... on #3, I've attached the work that the Fed/E&Y team put together on FP.. this narrowly addresses the FP issues and bankruptcy...we have another deck that begins to addresses the insurance company bankruptcy issues (I'll send that in a subsequent email) on #5. do you want E&Y to provide you with information on that or do you have the latest flash and can pull this together from that? on #6, we will also have an update (or are supposed to have one) from Brian Schreiber tonight that reflects an update on his best thinking on timing and valuation...we can send that as soon as (and if) we get it tonight on #7, we can have the ML 2 and ML 3 teams send their updated decks on these two structures....(recognizing that ML 3 keeps changing)....for tomorrow's discussion at 4:00/5:00, I'm not sure whether you got any sense from Jester, but my sense in talking with Tim was that we should start that discussion focused on the capital structure/Treasury $40B to get the consensus on that.....and keep the slides for the discussion focused on the solutions (inclusive of capital, ML 2 and ML 3) plus next steps, rather than the bigger deck that has all of the background information in it......let me know if you sense anything different from that from Jester?..... I'd like for Tim and others who will be participating on the 4:00 tomorrow to get information tomorrow morning as well.....I'll send you the list of folks that I expect will be participating from our side here's the systemic risk stuff for FP; the first is a summary document of exposures that highlights the different "channels" through with risk might be transmitted; the second is the portfolio-by-portfolio review of exposures summarized in the first document; the third is a LEH comparison (but ignores the difference in bankruptcy schemes applicable to LEH vs. FP)..... * * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * * * *

"Juhas, Peter (IBD)" <Peter.Juhas@morganstanley.com>

10/25/2008 04:38 PM

To

<sarah.dahlgren@ny.frb.org>, <amy.flynn@ny.frb.org>

cc

"Bischof, Eric (IBD)" <Eric.Bischof@morganstanley.com>, "Ryan, Kevin (GCM)" <Kevin.J.Ryan@morganstanley.com>, "Angelova-Makki, Anna (IBD)" <Anna.Angelova-Makki@morganstanley.com>.

Subject

Update on Dan Jester Call

I spoke to Dan Jester re what he is looking for. He said he would like us to prepare some materials for a meeting of the TARP oversight committee that go through various issues 1. Background of AIG situation - i.e., a background page on the company (i.e., largest insurance company in the world, operations in XX countries, $XXBn of CDS exposures, etc) and what events led to the first rescue - the downgrade and the resulting liquidity need in FP and securities lending business. - MS can put together2. Events between initial rescue and today that have led to a more difficult situation for the company - general financial markets declines, more difficult positions for many potential buyers, some deterioration in some of the businesses, more rapid draws than expected on the fed facility. - MS can put together3. Systemic risks today of an AIG bankruptcy - Sarah. I think that the Fed has put something together on this?4. Rating agency concerns - we can use the page that we are doing for the meeting tomorrow afternoon.5. Outlook for 3Q earnings and how are operating businesses performing?6. Asset disposition plan description. - we can use the pages that we had for the meeting/call on Thursday that discuss the plan.7. Summary of ML II and III - Sarah, not sure if you have something that is being put together internally that could be useful here?8. Proposed subordinated instrument description - term sheet.9. Pro forma capital structure - same page as we are putting together for tomorrow Fed discussion should suffice.He also said it would be helpful for him to have a discussion regarding the different considerations re preferred, sub debt, various fetaures, etc. We will try to get on phone with him Sunday am to discuss these. He told me that there is no reason why they would have to do similar features to the TARP preferred (i.e., the 9 pct coupon, cumulative preferred). He did think that a replacement capital covenant would be very difficult. We also spent some time discussing whether security would PIK or not - he had assumed cash pay and rate something like L+300, but we discussed why PIK may be more palatable for agencies to address coverage concerns.Dan said he would like us to get him something tomorrow. We will get started on these now, but Sarah if there is anything that you have on the items I noted above re systemic risks and ML II and III, can you let us know? Thanks.Pete [illegible] Any U.S. tax advice contained in the body of this e-mail was not intended or written to be used, and cannot be used, by the recipient for the purpose of avoiding penalties that may be imposed under the Internal Revenue Code or applicable state or local tax law provisions. The information contained in this message may be privileged and confidential and protected from disclosure. If the reader of this message is not the intended recipient, or an employee or agent responsible for delivering this message to the intended recipient, you are hereby notified that any dissemination, distribution or copying of this communication is strictly prohibited. If you have received this communication in error, please notify us immediately by replying to the message and deleting it from your computer. Notice required by law: This e-mail may constitute an advertisement or solicitation under U.S. law, if its primary purpose is to advertise or promote a commercial product or service. You may choose not to receive advertising and promotional messages from Ernst & Young LLP (except for Ernst & Young Online and the ey.com website, which track e-mail preferences through a separate process) at this e-mail address by forwarding this message to no-more-mail@ey.com. If you do so, the sender of this message will be notified promptly. Our principal postal address is 5 Times Square, New York, NY 10036. Thank you. Ernst & Young LLP - AIG FP Systemic Risk Summary OCT 20 08.doc - AIGFP

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Systemic Risk Matrix OCT 20 08.doc - AIG FP LEH Comparison OCT 20 08.doc - M0660487082977572900.pdf

tomorrow

Sarah Dahlgren

To:

Timothy Geithner, Thomas Baxter, Terrence Checki, Michael Silva, Meg McConnell

10/26/2008 12:21 AM

Cc:

Paul Whynott, Jim Mahoney, Steven.Manzari, Amy Flynn

Show Details

for tomorrow, we'd like to do two things: 1. We want to run you through the latest version of Maiden Lane 3 (CDS solution) -- in addition to explaining the current version of the structure, there are a couple of critical decision points that the team needs your input on (and that factor into timing issues in rolling out the package) .... we'd like to do this at 4:00 (the team will have a deck out tomorrow on this -- caveat is that it's midnight and we still don't have the numbers we need from BlackRock...but they are working on them....)2. As discussed on Friday evening, we will walk through the recommended structure on the capital and new FRBNY facility to get consensus with Treasury .... we asked Morgan Stanley late tonight for some additional scenarios (based on the cashflow meeting we had with the firm this evening) -- so the package with the solutions in it as described in the prior email will likely be coming around tomorrow morning.....we'd like to do this at 5:00 (assume this is with Jester?) Thanks.......* * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * * * *

Thomas Baxter/NY/FRS
10/26/2008 09:57 AM

To
Sarah Dahlgren/NY/FRS
cc

bcc

Subject
Re: tomorrow73022D4156851A12852576AF000F5215

Sounds good. I am in the office this morning but will not be here later on. Is there a dial in no. for these? Thanks.

Thomas C. Baxter, Jr.
General Counsel and Executive Vice President
Federal Reserve Bank of New York

Sarah Dahlgren/NY/FRS
10/26/2008 12:21 AM

To
Timothy Geithner/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS, Terrence Checki/NY/FRS@FRS, Michael Silva/NY/FRS@FRS, Meg McConnell/NY/FRS@FRS, Kristin Mayer/NY/FRS@FRS
cc
Paul Whynott/NY/FRS@FRS, Jim Mahoney/NY/FRS@FRS, Steven.Manzari@ny.frb.org, Amy Flynn/NY/FRS@FRS
Subject
tomorrow

for tomorrow, we'd like to do two things:

1. We want to run you through the latest version of Maiden Lane 3 (CDS solution) -- in addition to explaining the current version of the structure, there are a couple of critical decision points that the team needs your input on (and that factor into timing issues in rolling out the package) .... we'd like to do this at 4:00

(the team will have a deck out tomorrow on this -- caveat is that it's midnight and we still don't have the numbers we need from BlackRock...but they are working on them....)

2. As discussed on Friday evening, we will walk through the recommended structure on the capital and new FRBNY facility to get consensus with Treasury .... we asked Morgan Stanley late tonight for some additional scenarios (based on the cashflow meeting we had with the firm this evening) -- the package with the solutions in it as described in the prior email will likely be coming around tomorrow morning.....we'd like to do this at 5:00 (assume this is with Jester?)

Thanks........

* * * * * * * * * * * * * *
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Materials for 5pm meeting on Capital Structure

Amy Flynn

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o
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Timothy Geithner, Thomas Baxter, Terrence Checki, Christine Cumming, Michael Silva, Meg McConnell, Paul Whynott, Jim Mahoney, Steven.Manzari, dan.jester

10/26/2008 03:18 PM

Show Details

Please find attached materials for the 5pm meeting to discuss options for the capital structure and FRBNY facility. * * *Amy FlynnFederal Reserve Bank of New YorkOffice: 212-720-6431Cell: 347-266-4820 - 2008.10.26 Capital Structure Discussion Materials.pdf

Project Independence

Capital Structure Discussion Materials

26 October 2008

Executive Summary

Situation Overview

- Based on recent discussions among the rating agencies, AIG and the FRB, it appears likely that the senior unsecured debt of AIG, Inc. ("HoldCo") will be downgraded from A-/A3 (S&P/Moody's) in the near term unless AIG and the FRB take action
- The current financial profile of AIG does not fit the rating agencies' criteria for investment grade ratings as they are typically applied
- It is likely that projected losses in 3Q08 ($17-18Bn according to most recent company projections, including $11Bn related to other-than-temporary impairments) will be a catalyst for ratings action
- A downgrade to BBB would create significant liquidity issues at the HoldCo level (company estimates that a downgrade would create liquidity need of approximately $42Bn from CDO book and other areas of FP) and adversely impacts value of the insurance subsidiaries
- In order to achieve the objective of maintaining HoldCo and insurance company ratings, we believe that AIG will need to:
  - Mitigate or eliminate further downside in key risk areas (FP/CDS, RMBS portfolio, business deterioration)
  - Improve capital structure to levels acceptable to agencies given sell-down strategy in the interim
  - Demonstrate the viability and investment grade profile of AIG pro forma for completion of disposition plan

Executive Summary (cont'd)

Proposed Actions

- Given this situation, proposed FRB actions are as follows:

1) Implement ML II to address risks associated with RMBS portfolio
2) Implement ML III to address risks associated with FP ABS CDO portfolio
3) Restructure the rate, maturity and size of FRB facility
   - FRB facility would be partially refinanced through $40Bn issuance of a new subordinated instrument to the Treasury, with proceeds used to pay down FRB facility and [$25]Bn of facility permanently cancelled
4) Access to CPFF to provide access to additional temporary liquidity

- We believe the FRB should proceed with the proposed actions only if it has obtained sufficient comfort from AIG regarding compliance with the items listed on slide 17

Targeted Outcome

- Maintain current senior unsecured ratings per S&P and Moody's (A-/A3) and FSR ratings per A.M. Best (A)
- Minimize pressure on operating subsidiaries and retain value of key franchises
- Provide adequate interim liquidity to AIG
- Given the current environment and complexity of the situation, however, it is not possible to ensure that the ratings will not be subject to downgrade in the future, should further issues arise

Rating Agency Concerns

- Rating agencies' concerns focused on the following issues:
  - Current HoldCo capital structure
  - Execution risk associated with asset disposition plan
  - Ongoing liquidity and capital risks from FP
- The proposed FRB actions address these concerns by:
  - Reducing liquidity and capital risks associated with RMBS and FP ABS CDO portfolios
  - Reducing leverage and extending maturity of the FRB facility

The rating agencies have generally expressed concerns about the following issues:

- ***Asset Disposition Plan*** – The agencies would like to have a clear view of the asset disposition plan and get comfortable that the remaining company will be a going concern that can support its debt. All agencies are concerned that sale proceeds may be insufficient to cover the company's obligations, and that faster disposition may result in lower valuations.
- ***Leverage*** – Current leverage is considered too high for the present ratings. Nonetheless, the agencies generally deem the current capital structure temporary and note that of higher concern is the ability to pay down the debt through asset dispositions.
- ***Subordination of Senior Unsecured Debtholders*** – Generally, the rating agencies are concerned about the current subordination of the senior unsecured debt and the implications if asset sale proceeds are insufficient to repay the FRB loan.
- ***Facility Maturity*** – Generally, the agencies would view certain modifications to the FRB facility terms, such as extending the maturity, as a positive. Such modifications would provide the company with greater financial flexibility and additional time to complete the asset disposition plan, should the company need it.
- ***Cost of Capital*** – The rating agencies generally consider the current coupon rate on the FRB facility unsustainable. While the agencies understand that the high coupon is well aligned with the motivation of disposing assets and repaying the loan within a shorter period of time, they are concerned whether the proceeds from asset dispositions will be sufficient to pay down the loan principal and the PIK. Additionally, extending the maturity while maintaining the current coupon would be deemed particularly unconstructive.
- ***Financial Products*** – The agencies view FP as a major source of the company's problems and have indicated that they expect AIG and the FRB to take steps in the near term to minimize future liquidity and capital issues associated with the portfolio and to generally reduce exposures. If steps to address FP issues are not undertaken, the agencies believe that the company's liquidity problem will be prolonged and lead to further capital deterioration, which would require additional asset sales.

PRELIMINARY DRAFT

ML II Overview

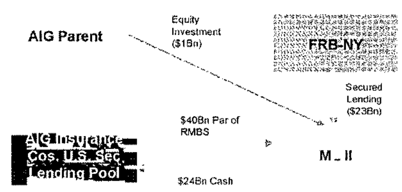
Based on BlackRock Analysis as of 10/23/2008

- ML II is designed to remove RMBS assets from the AIG balance sheet and mitigate further capital losses and liquidity pressures to AIG stemming from the RMBS portfolio
- ML II is a trust structure financed primarily by the FRB and cash from AIG
- The successful completion of ML II will allow for the termination of the FRB $37.8Bn Securities Lending program to AIG's U.S. insurance subsidiaries

FRB Objectives

- Ensure FRB-NY senior financing will be paid back even under severe stress scenarios
- Minimize cash drain on AIG parent
- Minimize capital hit to AIG (including Day 1 write-downs)
- Retain some upside to AIG (to satisfy rating agencies)
- Retain some upside to FRB-NY
- Consolidate off of AIG balance sheet

Proposed Structure



The proposed structure appears to meet key objectives

- ✓ Assumes $24 billion purchase price at AIG's marks
- ✓ High leverage to minimize cash drain on AIG: $1 billion equity, $23 billion senior debt
- ✓ Senior debt earns L+100—and immediately receives all cash flows until fully paid off (in 2013 in the base case)
- ✓ Equity earns L+300, which PIKs until debt is paid off (in 2013 in the base case)
- ✓ After equity is paid off, cash flows are split 5/6 to senior debt residual, 1/6 to equity residual
- ✓ Very low likelihood of failing to repay senior debt (P&I), even under severe stress scenarios
- ✓ Significant upside for FRB-NY (e.g., 14% IRR in base case)

MLII Portfolio Summary

($ in billions), As of 10/02/08

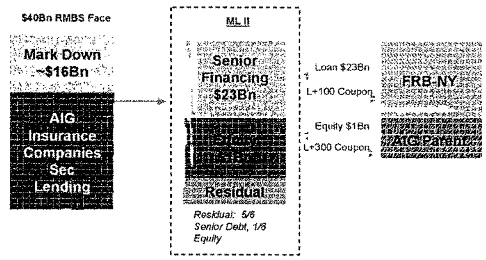
	Par	Market Value	Average Mark	% of Total Market Value
Subprime	$20.31	$13.70	0.67	57.05%
ALT-A	$15.61	$8.18	0.52	34.07%
HELOC	$1.39	$0.82	0.59	3.42%
Second Lien	$1.68	$0.78	0.46	3.25%
Jumbo Hybrid	$0.50	$0.25	0.50	1.04%
Other (Lot Loan, High LTV, Option ARM, Foreign Mortgages)	$0.36	$0.28	0.78	1.17%
Total	**$39.84**	**$24.01**	**0.60**	**100.00%**

Morgan Stanley

ML II Overview (cont'd)

Based on BlackRock Analysis as of 10/23/2008

Proposed Structure



Next Steps

- Impact of RMBS MTM volatility on FRB-NY B/S and consolidation
- Equity investment impact to AIG
- Completion of term sheet and other legal documents
- Other

Structural Commentary

	Transfer Price	Size of Equity vs. Debt	Terms of Debt and Equity	Origin of Equity
Proposed Option	• AIG marks as confirmed by BR, $24Bn at 9/30	• Equity—$1Bn • Loan—$23Bn • Residual—5/6, 1/6	• Equity—L+300 • Debt—L+100 • Debt full turbo paydown • Residual cash flows—5/6, 1/6	• AIG
Considerations	• Evaluate AIG Book marks and compare to estimates of current market values • Purchase price decision effects liquidity and capital of AIG and the senior financing facility	• Consolidation issues for AIG and FRB-NY • Smaller equity tranche means greater risk to Senior financing facility	• Lower coupon payments increase chance of principal paydown • Equity PIK strengthens Senior financing facility	• Alternative option - to sell equity and residual risk to third party

ML III Overview

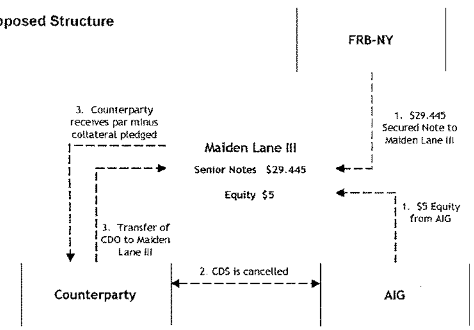
Overview

- Goal is to mitigate impairment of AIG capital and liquidity through:
  - Simultaneous tear-ups of CDS contracts between AIG FP and counterparties; purchase of ABS CDO reference assets by ML III from counterparties
  - Tear-up discussions with major counterparties ongoing

Open Issues

- Transfer Price – transfer at AIG's current marks minimizes adverse impact to AIG; adjusting to anticipated 10/31 collateral requests will result in an additional $4 billion reduction in collateral implied value
- Equity Structure – modeling equity from AIG in the form of cash, securities or a derivative (commitment to pay by year-end 2009, secured by unencumbered assets)
- Equity Size – BlackRock is modeling structure with additional equity protection to the Fed; increase in equity tranche potentially raises consolidation issues
- M-T-M Volatility – Potentially very large M-T-M to FRBNY
- Counterparty Negotiations – need to negotiate trade tear-ups and, potentially, negotiate concessions (1 to 2 points appears feasible)

Proposed Structure



Counterparties

	Exposure	Coll Posted	Coll Implied Value	BLK Value	Extreme Stress PV	Concession
Societe Generale	16,546	8,327	8,219	8,059	9,455	(326)
Goldman Sachs	14,547	7,186	7,361	6,500	8,662	(271)
Merrill Lynch International	6,377	3,135	3,241	2,963	3,124	(128)
Deutsche	5,395	2,809	2,586	3,051	5,345	(29)
Calyon	4,336	2,289	2,047	1,968	2,217	(65)
UBS	4,218	1,457	2,761	1,977	2,606	(69)
Barclays	2,455	1,293	1,162	1,179	1,592	(23)
Coral Purchasing (DZ Bank)	1,815	734	1,080	831	1,041	(33)
Bank of Montreal	1,389	504	886	663	911	(36)
Rabobank	1,174	636	539	588	825	(13)
Royal Bank of Scotland	1,138	624	513	548	699	(25)
Bank of America	776	247	529	397	392	(12)
Wachovia	775	134	641	432	503	(23)
HSBC	596	264	332	299	463	(3)
BGI (Cash Equivalent Fund II)	125	37	87	35	26	(1)
Other	2,461	-	2,461	1,631	2,403	(15)
Total	**64,121**	**29,676**	**34,445**	**31,121**	**40,262**	**(1,093)**

Overview of FRB Facility Restructuring

- Terms of the current $85Bn FRB facility are as follows:
  - Senior secured facility
  - Maturity: 2 years
  - Drawn rate: L+850 bps, PIK
  - Undrawn rate: 850 bps, PIK
- In order to address rating agencies' concerns, proposal is to restructure and refinance the facility as follows:
  1) Senior secured facility of $[45-60]Bn
     - Maturity: [5] years
     - Drawn rate: [L+300] bps, PIK
     - Undrawn rate: [50-75] bps, PIK
  2) Treasury subordinated instrument of $40Bn designed to receive high equity credit from the rating agencies and used to pay down a part of the FRB facility
     - Could be structured either as cumulative preferred stock similar to securities that have been issued through TARP or subordinated debt instrument
     - We believe that, if available, a subordinated debt instrument would be preferable because it would receive higher equity credit from the rating agencies and would be *pari passu* with the existing AIG hybrids

PRELIMINARY DRAFT

[redacted]

Comparison of Capital Alternatives

	Senior Preferred Stock	Proposed Junior Subordinated Debt
Rank	Senior to common stock and pari passu with existing preferred shares	Subordinated to all senior debt but pari passu with other hybrid debt and trade creditors
Upside participation: Warrants	None, other than existing 79.9%	None, other than existing 79.9%
Maturity	Perpetual	Final: 60 years \ Scheduled: 50 Years
Replacement Capital Covenant	Prior to Year 3, Senior Preferred may only be redeemed with the proceeds from qualifying preferred stock and common stock, in whole or in part but not less than 25% of the notional at issuance; covenant is eliminated upon achievement of ratios to be determined	The issuer will be obligated to redeem the notes only with proceeds raised from the sale of securities that receive the same or better equity credit (determined at the time of redemption); covenant is eliminated upon achievement of ratios to be determined
Issuer's Call Option	Callable at anytime at Par	NC-5
Div dend / Coupon Ra e	[9]% per annum; PIK	[9]% per annum; PIK payable during first 5 years
D v dend / Coupon Deferral	Freely deferrable, deferred dividends accumulate and compound	Deferrable for up to 10 consecutive years, dividends accumulate and compound. Deferred must be repaid from the sale of common stock, qualifying warrants or non-cumulative perpetual preferred stock. Such sales are mandatory after the 5th year of optional deferral
D v dend Stopper	During any deferral period and until such time all accumulated interest payments are paid in full, no dividends or repurchases shall be made on any capital stock or securities that rank pari passu or junior to the senior preferred stock Prior to Year 3, if preferred shares still outstanding no increase in common stock dividend is permitted without consent from the U.S. Treasury	During any deferral period and until such time all accumulated interest payments are paid in full, no dividends or repurchases shall be made on any capital stock or securities that rank pari passu or junior to the notes
Lende s' Cla m n Bankruptcy	Equity claim with liquidation preference to common equity claim	Creditors' claim (subordinated)
Lende s' Acceleration Rights	None	Failure to pay interest when due (subject to deferral provisions) + bankruptcy
Equity Treatment	S&P: 100% equity credit up to 15% of Capital Moody's: __ A.M. Best: [75%] equity	S&P: 100% equity credit up to 15% of Capital Moody's: Basket "[C]" [50]% equity A.M. Best: 75% equity
Tax Treatment	Non tax-deductible to AIG	Tax-deductible to AIG
Balance Sheet Presentation	Shareholders' Equity – allocation between preferred equity and APIC (for pro-rata fair value of warrants)	Junior subordinated long-term debt

Benefits of Proposed Junior Subordinated Debt

- Maintains debt claim in bankruptcy while achieving significant rating agency equity credit: [50]% equity credit at Moody's, 100% equity credit up to 15% of capital at S&P
  - While a mandatory convertible into common would provide up to 25% of capital at S&P and Basket "D" at Moody's, the holder would be forced to convert into common stock at Year 3
- Both subordination level and interest rate superior to TARP Preferred Stock

Term Sheet

Junior Subordinated Loan

- The Junior Subordinated loan will rank pari passu to the following securities:
  - $1,000,000,000 aggregate principal amount of 6.25% Series A-1 Junior Subordinated Debentures
  - £750,000,000 aggregate principal amount of 5.75% Series A-2 Junior Subordinated Debentures
  - €1,000,000,000 aggregate principal amount of 4.875% Series A-3 Junior Subordinated Debentures
  - $750,000,000 aggregate principal amount of 6.45% Series A-4 Junior Subordinated Debentures
  - $1,100,000,000 aggregate principal amount of 7.70% Series A-5 Junior Subordinated Debentures
  - $4,000,000,000 aggregate principal amount of 8.175% Series A-6 Junior Subordinated Debentures
  - $5,880,000,000 aggregate principal amount of Series B-1, B-2 and B-3 subordinated debentures and purchase contracts
  - €750,000,000 aggregate principal amount of 8.000% Series A-7 Junior Subordinated Debentures
  - £900,000,000 8.625% Series A-8 Junior Subordinated Debentures

Borrower/Issuer.	AIG Inc.
Lender:	The United States Department of The Treasury
Anticipated Ratings:	Moody's: Baa1 / S&P: BBB / A.M. Best: bb+
Rank:	Subordinated to all senior debt. Pari passu with other hybrid debt and trade creditors
Final Maturity:	60 years
Scheduled Maturity:	50 years
Replacement Capital Covenant (RCC):	The issuer will be obligated to redeem the notes only with proceeds raised from the sale of securities that receive the same or better equity credit (determined at the time of redemption); covenant is eliminated upon achievement of ratios to be determined
ssuer's Call Option:	NC-5 at Par
Div dend / Coupon Rate:	[9]% per annum; PIK payable during first 5 years
Optional Doforral:	Cumulative and compounding at Issuer's discretion for up to 10 consecutive years If optional deferral period exceeds 1 year, in the year following the end of the optional deferral period the issuer may not repurchase common stock
A ternative Payment Mechanism (APM):	Deferred interest is to be repaid from the sale of common stock, qualifying warrants (with exercise price above current equity price) or non-cumulative perpetual preferred stock. APM is mandatory after 5 years of optional deferral
APM Cap:	The warrants are capped at 2% of total number of issued and outstanding shares. Preferred stock is capped at 25% of the principal amount for the life of the security. Warrant cap expires 5 years after the commencement of a deferral period
Share Cap:	Issuer is not required to issue qualifying warrants that exceed [•] million shares. Issuer must use commercially reasonable efforts from time to time to increase the share cap to a number of shares that would allow issuer to satisfy deferred interest via APM
Dividend Stopper:	During any deferral period and until such time all accumulated interest payments are paid in full, no dividends or repurchases shall be made on any capital stock or securities that rank pari passu or junior to the notes
nterest Forgiveness in Bankruptcy:	Excess of 2 years of unpaid and compounded interest
Events of Default:	Failure to pay interest when due (subject to deferral provisions) , certain events of bankruptcy, insolvency or reorganization and failure to pay principal when due
Moody's / S&P Equity Credit:	S&P: 100% equity credit up to 15% of Capital Moody's: Basket "[C]" [50]% equity

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Pro Forma Capital Structure

Rating Agency Metrics

- Leverage at 9/30/08 is well above rating agencies' guidelines for investment grade ratings
- Leverage ratios are substantially lower with subordinated instrument that receives high equity credit from the rating agencies

Leverage Metrics

P&C / Life Insurance

Category	Moody's	S&P
AAA	< 20%	< 15%
AA	20–30%	15–25%
A	30–40%	25–35%
BBB	40–50%	35–45%
BB	> 50%	45–65%

Max Hybrid + Preferred

S&P	15%

GAAP Int. Coverage Metrics

P&C / Life Insurance

Category	Moody's	S&P
AAA	> 12x	> 10x
AA	8–12x	8–10x
A	4–8x	5–8x
BBB	2–4x	3–5x
BB	< 2x	2–3x

Pro Forma Capital Structure

$Bn

			$45Bn FRB Facility		$60Bn FRB Facility	
	6/30/2008	PF 9/30/2008	PF 9/30/2008 Reflects Restructuring With Lower Equity Credit	PF 9/30/2008 Reflects Restructuring With Higher Equity Credit	PF 9/30/2008 Reflects Restructuring With Lower Equity Credit	PF 9/30/2008 Reflects Restructuring With Higher Equity Credit
Capitalization						
FRB Facility [1]	-	85.0	45.0	45.0	60.0	60.0
Existing Senior Debt (Net)	15.4	16.9	16.9	16.9	16.9	16.9
Hybrid	12.9	12.9	12.9	12.9	12.9	12.9
Mandatory Convertible	5.9	5.9	5.9	5.9	5.9	5.9
Treasury Subordinated Instrument - 50% Equity Credit	-	-	-	40 0	-	40.0
Treasury Subordinated Instrument - 25% Equity Credit	-	-	40.0	-	40.0	-
Equity (ex. AOCI)	82.0	56.3	56.3	56 3	56.3	56.3
Minority Interest	11.1	11.1	11.1	11.1	11.1	11.1
Total Capital (ex. AOCI)	**127.3**	**188.1**	**188.1**	**188.1**	**203.1**	**203.1**
Adjusted Moody's Leverage (ex. AOCI) [2]	**19 7%**	**58.1%**	**52.9%**	**47.8%**	**56.3%**	**51.5%**
Adjusted S&P Leverage (ex. AOCI) [3]	**12.1%**	**54.2%**	**32.9%**	**32.9%**	**37.9%**	**37.9%**
Implied Ratings Based on Leverage Guidelines	*AAA*	*BB*	*BB / A*	*BBB / A*	*BB / BBB*	*BB / BBB*
Hybrid + Treasury Subordinated Instruments / Total Capital	*14.7%*	*10.0%*	*31.2%*	*31.2%*	*28.9%*	*28.9%*
Adjusted S&P Leverage (ex. AOCI)	12.1%	54.2%	49 2%	49.2%	51.8%	51.8%
EBIT / Interest Expense [4] [5]	**10.4x**	**1.9x**	**2 6x**	**2.6x**	**2.4x**	**2.4x**
EBIT / Interest Expense (ex. PIK Interest) [4] [5]	**10.4x**	**10.4x**	**10.4x**	**10.4x**	**10.4x**	**10.4x**
Implied Ratings Based on Coverage Guidelines	*AA / AAA*	*BB*	*BBB / BB*	*BBB / BB*	*BBB / BB*	*BBB / BB*

Notes

1 Assumes facility is fully drawn at 9/30/08

2 Adjusted for debt treatment of $6Bn in Pension and Lease obligations, assumes 75% equity credit for Hybrid and Mandatory Convertible, assumes 50% equity credit for Treasury Subordinated Instrument – 50% Equity Credit, assumes 25% equity credit for Treasury Subordinated Instrument – 25% Equity Credit

3 Assumes S&P treats Treasury Subordinated Instruments as equity, which requires relaxation of max hybrid constraint (up to 15% of total capital)

4 2009E EBIT of $23 2Bn (based on 10/14/08 Management model)

5 PF 9/30/08 rates 12 0% pre-tax interest rate on FRB Facility (LIBOR + 8 5%)
PF 9/30/08 restructured rates 6 5% pre-tax interest rate on FRB Facility (LIBOR + 3%), 9 0% pre-tax interest on Treasury Subordinated Instruments

Morgan Stanley

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FRBNY-TOWNS-R1-135063

Tentative Timetable

- Sunday, October 26, 2008: FRB and Treasury consensus on structure of Treasury investment
- Monday, October 27, 2008: Discuss Treasury investment with AIG management
- Tuesday and Wednesday, October 28 and 29, 2008: Discussion with rating agencies
- Monday, November 3, 2008: Approval of AIG recapitalization and restructuring plan by the AIG Board of Directors, the TARP Board of Directors and the Federal Reserve Board of Governors; Public announcement
- Tuesday, November 4, 2008: Election Day
- Wednesday, November 5, 2008: AIG files 10-Q
- Thursday, November 6, 2008: AIG earnings call

Next Steps

- Continue working with AIG
- Engage / negotiate with the rating agencies
- Target for announcement on [November 5], concurrent with earnings release
- Work on draft press release / communication plan

Appendix A

Appendix

Moody's Treatment of Hybrid Securities

Non-Dilutive Fixed Income Hybrids: Tax-deductible Structures

- Moody's assigns equity credit based upon 3 factors:
  - Maturity
  - Ongoing payment obligations
  - Loss Absorption
- The grid shows the category ratings and Basket for recent tax-deductible hybrid deals

  "A" = 0% Equity Credit

  "B" = 25%

  "C" = 50%

  "D" = 75%

  "E" = 100%

Assumption: Moderate on Loss Absorption (Jr. Subordinated Debt that is pari passu with trade creditors)

No Ongoing Payments		Maturity: **Weak** 30-50 years and intent to replace 50+ years	Maturity: **Moderate** 30-50 years and RCC 50+ years and intent to replace	Maturity: **Strong** 50+ years and RCC
Weak	10 years of Optional Deferral			**C** 60 years and covenant to replace AEP, Xcel Energy, GECC, Enbridge Energy, FPL, CVS, Enterprise Products, Teppco Partners LLP, Wisconsin Energy, US Bancorp
Moderate	10 years of Optional Deferral [1] -stock/warrant sales after year 5 -investors take some risk on deferred interest[2]		**C** 60-80 years and intent to <u>replace</u> PNC, Morgan Stanley, Wachovia, Partner Re, Transcanada **With or without the springing covenant**	**D** 60-80 years and covenant to <u>replace</u> AIG, Progressive, Webster Financial, BB&T, StanCorp, Delphi Financial, Nationwide, Huntington, Allstate, State Street, Chubb, Travelers, Liberty Mutual, Comerica, Ambac, Textron
Strong	Mandatory Equity Sales upon breach of Triggers -investors take some risk on deferred interest[2]	**C** 40 years and intent to replace Stanley Works	**D** 40-50 years and covenant to <u>replace</u> BNSF, Great West Life 60 years and intent to replace Lehman Brothers, RGA, Zurich Financial, International Lease, Lincoln National, Amenprise,	**D** 60 years, mandatory triggers and covenant to replace MetLife

Notes

1 If Issuer defers for more than 1 year, issuer may need to wait 1 year following the conclusion of the deferral period before repurchasing or redeeming equal or more junior securities

2 E.g., in bankruptcy investors have a claim on only the first two years of deferred interest

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APPENDIX

S&P Treatment of Hybrid Securities

Equity Credit Spectrum

- AIG's existing debt hybrids receive intermediate equity content up to 15% of Capital
- AIG's mandatory convertibles into common receive high equity content up to 25% of Capital

S&P allocates hybrid instruments into each of its three baskets to the extent that they replicate its four dimensions of equity credit:

No Maturity: the long datedness of the instrument and ability to avoid repayment obligation; to receive Intermediate credit, subordinated debt must have a maturity of at least 20 years

No Ongoing Payments: ability to defer coupon payments; to receive Intermediate credit, no requirement to sell stock within first 5 years of deferral (subject to limited exceptions)

Creditors' Cushion: subordination in the capital structure, ability to absorb losses; to receive Intermediate credit, should be deeply subordinated

Permanence in the Capital Structure: replacement call obligations; S&P has indicated that a 100 bps or less step-up can still qualify for Intermediate credit with an RCC

S&P Hybrid Spectrum

	Minimal Equity Content	Intermediate Equity Content	High Equity Content
Equity Credit:	0%	100% up to 15% of Capital	100% up to 25% of Capital
	e.g. non-deferrable subordinated debt[2]	Perpetual preferred stock and most tax-deductible hybrids	3 year mandatory convertibles into common stock

Implications of basket treatment for ratio purposes:

Minimal Equity Content: instrument assumed to be debt for ratio purposes

Intermediate Equity Content: ratios calculated assuming 50% debt and 50% equity

High Equity Content: instrument assumed to be equity for ratio purposes

Notes
1 For the purpose of calculating hybrid equity tolerances for U.S. and Bermuda-based insurance companies, "Capital" is defined as total common equity, preferred shares and other hybrid securities, minority interest, and debt less unrealized appreciation (depreciation) on fixed-income securities
2 For hybrids with interest deferrals. Within 10 years of the repayment date, S&P will gradually treat the instrument as more debt-like, using a 5 year amortization schedule whereby for each year under 10 years an incremental 20% of the instrument is treated like debt until at 5 years of remaining life, the issue is viewed as completely debt like

Additional Requirements on AIG / Conditions to Treasury Investment

- Satisfactory liquidity plan with credible estimates regarding future needs to access FRB facility, as well as assessment of potential risks to this plan
- Wind-down plan for FP that mitigates future liquidity needs and capital risks and reduces size of business as expeditiously and efficiently as possible
- Asset disposition plan that presents viable AIG core business post-dispositions
- Changes to AIG Board of Directors
- Compliance with new expenditure policies and procedures
- Executive compensation restrictions under EESA (see next page)

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APPENDIX

Executive Compensation Limits under EESA

Executive Compensation Limits Under TARP – CCP, Imposed on the 9 Participating Banks

- **Institution must limit senior executive severance benefit to less than 3 times executive's average taxable compensation for 5 years preceding termination**
  - Limit applies to severance benefits triggered by:
    - Involuntary termination
    - Termination in connection with bankruptcy, insolvency or receivership
  - Limit applies to CEO, CFO and next 3 most highly compensated executive officers ("SEOs")
- **Institution must limit to $500,000 per SEO its annual deduction for compensation**
  - No exception for performance-based compensation
  - Deferral does not avoid the deduction limit – excess amount non-deductible when paid
- **Institution must require clawback of SEO bonus and incentive payments based on financial statement/ performance metrics later determined materially inaccurate**
  - Accounting restatement not required
  - Misconduct not required
- **Institution must eliminate incentives for SEOs to take unnecessary and excessive risks**
  - Institution's compensation committee (or similar board committee) must:
    - Promptly (within 90 days) review its SEO compensation arrangements with its senior risk officer (or other like personnel) to ensure arrangements do not encourage SEOs to take unnecessary and excessive risks
    - At least annually discuss and review with the senior risk officer to the relationship between institution's risk management policies/practices and SEO incentive compensation arrangements; and
    - Certify annually that it has complied with the above
  - Public institutions must include the annual certification in the institution's annual proxy statement Compensation Discussion and Analysis

Additional/Alternative Executive Compensation Limitations under Other TARP Programs

- **Program for Systemically Significant Failing Institutions**
  - CPP rules continue to apply to CPP participants, plus absolute prohibition on severance payments to SEOs

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Re: Do you think 000000000003FFFF006E001372080000

Michael S Gibson

To: Jon D Greenlee, Kieran Fallon, Rich Ashton, Sarah Dahlgren, Steven J Manzari

11/03/2008 11:49 PM

Sent by: Michael S Gibson@BOARD

Show Details

468

Rich,

I made those changes. I also took out the various bracketed placeholders asking questions. The new version is attached.

Mike

systemic-risks-of-aig-for-treasury.doc

Michael S Gibson/BOARD/FRS

11/03/2008 07:27 PM

To
Rich Ashton/BOARD/FRS@BOARD, Sarah Dahlgren/NY/FRS@FRS

cc
Jon D Greenlee/BOARD/FRS@BOARD, Kieran Fallon/BOARD/FRS@BOARD, Steven J Manzari/NY/FRS@FRS

Subject
Re: Do you think

Rich,

I don't know which version you have.

I will add a "confidential" label to the top of each page in place of Restricted FR, and I will add a footnote on the first page with your point that this is a staff product. If there are any other formatting changes that are needed, let me know.

I'll make the changes later tonight when I have my laptop out.

Mike

----- Original Message -----
From: Rich Ashton
Sent: 11/03/2008 07:01 PM EST
To: Sarah Dahlgren
Cc: Jon Greenlee; Kieran Fallon; Michael Gibson; Steven Manzari
Subject: Re: Do you think

Keiran and I spoke with Scott. He is O.K. with sending the staff memo on the systeic consequences of an AIG defalt it to Treasury provided it is marked confidential and Treasury understands that they must keep it confidential and provided we make clear that this is a staff product and does not represent anyformal finding by the Board about systemic effect, like the one the Board recently made under the FDI Act. I'm not sure that I have the final version. Mike, if what you sent me is the final I can make sure it gets to Matt Rutherford at Treasury or New York can send it if that's easier.

Sarah Dahlgren/NY/FRS@FRS

11/03/2008 05:21 PM

To
Kieran Fallon/BOARD/FRS@BOARD, Rich Ashton/BOARD/FRS@BOARD, Michael S Gibson/BOARD/FRS@BOARD, Jon D Greenlee/BOARD/FRS@BOARD

cc
Steven J Manzari/NY/FRS@FRS

Subject
Re: Do you think

Understand! Thanks much.....
Sarah Dahlgren
Senior Vice President
Federal Reserve Bank of New York
Office: 212-720-7537
Cell: 917-770-8147

469

Sent from my BlackBerry Handheld.

----- Original Message -----
From: Kieran Fallon
Sent: 11/03/2008 05:19 PM EST
To: Sarah Dahlgren; Rich Ashton; Michael Gibson; Jon Greenlee
Cc: Steven Manzari
Subject: Re: Do you think

We're waiting to hear from Scott, which is why we didn't jump in during the discussion.

Kieran

--Sent from my BlackBerry Wireless Handheld

----- Original Message -----
From: Sarah Dahlgren
Sent: 11/03/2008 05:19 PM EST
To: Rich Ashton; Kieran Fallon; Michael Gibson; Jon Greenlee
Cc: Steven Manzari
Subject: Do you think

It's possible to share Mike's memo on AIG with Treasury?......
Sarah Dahlgren
Senior Vice President
Federal Reserve Bank of New York
Office: 212-720-7537
Cell: 917-770-8147

Sent from my BlackBerry Handheld.

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Systemic risks of AIG[1]

November 3, 2008

Introduction

In this memo, I discuss the possible systemic risks from a failure of AIG. The particular scenario considered is a bankruptcy filing by AIG, Inc., the parent holding company, and AIG Financial Products Corp. (AIGFP), with AIG's insurance subsidiaries entering a rehabilitation process overseen by domestic and foreign regulators. Much of the information used to prepare this memo was provided by management representations at AIG. In many cases, information is incomplete and the memo's conclusions should be viewed as preliminary.

Market confidence

The largest systemic risk at present is the risk to market confidence from a failure of AIG. Market confidence is in a fragile state after the intense financial turmoil of recent weeks. Treasury and the Federal Reserve have taken a range of actions, including the initial decision to lend to AIG. A broadening of government support for financial institutions has appeared to help stop the loss of market confidence in the financial system. A failure of AIG would call into question the ability of that broader government support to be sustained. This risk is impossible to quantify.

Exposures to AIGFP

AIGFP, AIG's capital markets and derivatives subsidiary, contains a number of systemic risks. I describe six of the important risks below. Given the range of risks present within AIGFP, there are undoubtedly some important risks that have been omitted from this list.

1. CDS written on ABS CDOs

AIGFP wrote credit protection on super-senior tranches of ABS CDOs and is exposed to the subprime mortgage-backed securities that the ABS CDOs own. The current notional amount of AIG's positions is $71 billion. AIG has taken $33 billion of writedowns on these positions as of September 30, 2008 and has posted collateral to its counterparties of $33 billion.

If AIG fails, its counterparties would face a loss on whatever uncollateralized exposure exists at that time. Counterparties have marked these positions down by $4 billion since September 30 (for a cumulative mark-to-market of $37 billion) and are currently asking for that amount of additional collateral. AIG is disputing those marks

[1] This memo is a staff product and does not represent any formal finding by the Board about systemic risk effects.

and has not posted the additional collateral. If AIG fails, its counterparties would bear the $4 billion loss.

Many of the counterparties own the underlying CDO securities against which AIG wrote credit protection or have other hedges. They would be left with up to $38 billion of unhedged super-senior ABS CDO risk if AIG failed. Because these positions are extremely sensitive to further house price declines, it would be expensive for AIG's counterparties to replace these positions. This would cause additional losses beyond the $4 billion described above.

At the time of the September 16 loan, the notional value of CDS written on ABS CDOs was $80 billion. AIG had taken $25 billion of writedowns as of June 30 and had posted $16 billion of collateral, leaving AIG's counterparties with an exposure of $9 billion. Systemic risk has fallen since September 16 because AIG has drawn on the Federal Reserve's $85 billion facility to post collateral against this $9 billion.

2. Regulatory capital arbitrage CDS

AIG wrote credit protection on super-senior tranches of corporate loan and prime mortgage exposures held by European banks in order to provide those banks with a regulatory capital reduction under their national implementations of Basel 1 capital standards.[2] AIG's largest counterparties are French, German, Dutch, Danish and Swedish banks. The notional amount outstanding has fallen from $379 billion at year-end 2007 to $240 billion at October 13, 2008. The portfolio is running off quickly because the counterparties have the option to terminate the trades when they go live onto Basel 2. The capital relief for AIG's European bank counterparties is currently estimated at between $2.4 and $11.1 billion, depending on where each bank's transition from Basel 1 to Basel 2 stands.[3] AIG's current mark-to-market loss is only $160 million, reflecting the fact that these trades were structured to transfer no credit risk, merely to provide regulatory capital relief.

If AIG fails, the Basel 1 risk-weighted assets reported by its counterparties would increase, resulting in a regulatory capital hole of up to $11.1 billion. Although the market knows this aggregate amount already from AIG's public disclosures, AIG's failure would reveal to the market which particular banks had shored up their Basel 1 capital ratios in this way.

Compared with the time of the September 16 loan, systemic risk is lower because the notional amount of trades is lower (it was $305 billion on June 30) and because European governments have put measures in place to guarantee bank liabilities and inject capital into banks.

[2] These trades would not have provided capital relief under the U.S. implementation of Basel 1 capital standards.
[3] To avoid shouting "Fire!" in a crowded theater, we have not approached the European regulators to quantify the capital relief more precisely.

3. Intra-company exposures to AIGFP[4]

AIG's other subsidiaries have material exposures to AIGFP on OTC derivatives. The largest exposures are at finance company affiliates ($920 million) and the funds management affiliate ($441 million). Insurance affiliates are owed approximately $475 million. In addition, these affiliates would have to replace these hedges (primarily interest rate and foreign currency derivatives) at a time when markets are volatile.

A default of AIGFP would have a catastrophic impact on Banque AIG, a French bank that is a wholly-owned subsidiary of AIGFP and through which AIGFP executed many of its OTC derivative trades. For example, Banque AIG is the counterparty to the European banks' regulatory capital trades. All the exposures in Banque AIG's trades are hedged with back-to-back trades with AIGFP.

Systemic risk from these intra-company exposures is high. In particular, the failure of Banque AIG (a regulated bank) could have a more damaging effect on market confidence than the failure of AIGFP (an unregulated derivatives product subsidiary). Through the intra-company exposures, the failure of AIGFP would cause significant loss of value at AIG's other subsidiaries, many of which are expected to be sold to repay the Federal Reserve's loan.

4. Stable value wraps

AIGFP has provided stable value wraps, referred to as Benefit Responsive Options (BROs), for 401k plan participants. AIG guarantees that plan participants can receive book value for qualified withdrawals, although AIG is not required to make any payments until after a fund's assets are depleted through qualified withdrawals. AIG had a notional value of $36 billion of BROs at September 30, 2008 with 175 plan counterparties. The aggregate market-to-book ratio was estimated at 95.5 percent at September 30, leaving AIG with an exposure of $1.6 billion.

Systemic risk of these stable value wraps is high. Although the exposure amount is not large and it is unlikely that AIG will have to make any payments, market confidence would be affected if plan sponsors are forced to notify plan participants that their investments in stable value funds are no longer guaranteed (at the same time that turmoil in credit markets is pushing down the market value of the funds' investments). This risk is falling over time, as plan sponsors replace AIG as the stable value wrap counterparty when contracts are renewed. Deals with aggregate book value of $3.3 billion were terminated before September 30.

5. AIGFP's liabilities

Some of AIGFP's liabilities may pose a systemic risk. These include guaranteed investment contracts (GICs) and debt securities. GICs have been issued to a variety of counterparties including municipalities. AIGFP has $11.4 billion of GICs outstanding, of

[4] This section relies on analysis done by John Kambhu.

which $9.7 billion is collateralized. Much of AIGFP's $35 billion outstanding of debt securities was structured to provide a counterparty with a market risk exposure (to interest rate, equity, commodity, or foreign exchange rate risk). Some was sold to banks and institutional investors who passed the market risk through to individual high net worth investors, and some was sold directly to investors who are exposed to an AIG default.

Systemic risk on GICs has fallen considerably since September 16, when GICs outstanding were $19 billion, of which about $12 billion was uncollateralized. Only $1.7 billion of uncollateralized exposure on GICs remains. Systemic risk on debt securities is still high, as these have a longer maturity and no collateral requirements. If AIG defaults, AIGFP's counterparties on structured notes – banks and institutional investors – would suffer a direct loss of principal and would also be left with an open risk position vis-à-vis their customers to whom they passed through the market risk exposures. While AIG's counterparties have had ample opportunity to hedge their exposure to an AIG default, we do not know who the counterparties are or whether they have hedged.

6. OTC derivatives

Some of AIGFP's OTC derivatives counterparties have uncollateralized exposures that would result in a loss if AIG defaults. The most recent data available on derivatives payables as of September 23 showed the top 50 counterparty exposures summed to $4.5 billion. The largest exposures were to securitization trusts (for interest rate swaps that enable the trust to match the interest rate risk of its assets and liabilities), financial institutions, corporates, and sovereigns.

Systemic risk may be highest for the securitization trusts and financial institutions. Many investors in mortgage-backed securities or asset-backed securities would be surprised to learn that an AIG default could have an impact on their investment, since securitization trusts are designed to be "bankruptcy remote," which could have knock-on effects in broader securitization markets. Lehman Brothers also had OTC derivatives outstanding with a large number of securitization trusts. As a result of Lehman's bankruptcy, many of those transactions have been downgraded by rating agencies, and investors may suffer losses.

Financial institutions that reported a material loss to AIG on OTC derivatives could suffer a loss of market confidence. However, most of AIG's counterparties with large OTC derivatives exposures are European banks whose governments have already put in place extraordinary measures to support their national banking systems.

If AIG fails and its OTC derivatives book is unwound, counterparties would be forced to replace their positions with AIG or retain an unhedged risk position. When Lehman Brothers failed, this was a major concern, but rehedging of Lehman's OTC derivatives did not turn out to have systemic effects. Lehman's OTC derivatives book was ten times larger than AIG's (measured by notional amount) which suggests that this risk may not be large.

However, to the extent that AIG's book of OTC derivatives has a different character than Lehman's, there may be additional systemic risk concerns. Some of AIG's OTC derivatives trades are different because they were done solely to exploit AIG's AAA rating. For example, AIG is an intermediary on a set of 30-year natural gas swaps between Goldman Sachs and the Southern California Public Power Authority (which provides electricity to Los Angeles and other cities in Southern California). Presumably the Power Authority was uncomfortable with Goldman Sachs as counterparty on a 30-year trade and was willing to pay a premium for the comfort of an AAA-rated counterparty. AIG's failure would leave both counterparties with a large open risk position that they would need to rehedge (presumably they could rehedge with each other). In addition, AIGFP also has an exotic derivatives book whose positions could prove difficult for counterparties to replace in current market conditions.

Another systemic risk consideration is the operational burden on OTC derivatives markets of coping with the default of a large counterparty who is also a common reference entity in CDS. The Lehman Brothers default strained the market's operational capacity, but the fear that operational failures would cause systemic risks did not materialize. However, the market may not have had the capacity to simultaneously cope with an AIGFP bankruptcy and a Lehman Brothers bankruptcy. This aspect of systemic risk from AIG has fallen, since more than a month has passed since Lehman's bankruptcy.

Commercial paper

AIG, AIGFP, and two of AIG's finance subsidiaries have $6.9 billion of commercial paper outstanding as of October 22, 2008. Of the $6.9 billion, $4.2 billion is asset-backed commercial paper (ABCP) and the remainder is unsecured. The bankruptcy of Lehman Brothers demonstrated how commercial paper held by money market mutual funds could pose a systemic risk. We do not know who is holding AIG's commercial paper, but presumably this risk is still high.

However, the systemic risk from AIG's commercial paper has diminished since September 16, when AIG had $19.7 billion of CP outstanding. Of the $19.7 billion, $5.1 billion was ABCP. Since then, the Federal Reserve has established three lending facilities (AMLF, CPFF, and MMIFF) to reduce the systemic risk related to commercial paper and money market mutual funds.

Securities lending

AIG still has approximately $20 billion of borrowings from banks and broker-dealers remaining in its securities lending program. If AIG fails, the securities lending counterparties could receive ownership of the securities in lieu of receiving their cash. These securities are high-grade corporate bonds and agency MBS, so credit losses are not expected, but this could have a material funding impact on those counterparties.

However, the systemic risk impact of the securities lending program is lower now than it was on September 16, when AIG had approximately $69 billion in liabilities and funding markets were under tremendous strain from the Lehman Brothers bankruptcy. The amount outstanding has fallen as counterparties have refused to roll over their securities lending transactions with AIG. A wider array of Federal Reserve lending facilities to support short-term funding markets is now available to help AIG's counterparties deal with the funding impact of an AIG default.

Insurance subsidiaries

AIG's regulated insurance subsidiaries, both domestic and foreign, would be affected by the default of the AIG parent holding company. State regulators have stated that the insurance companies they regulate are capitalized on a stand-alone basis and can maintain claims-paying ability to benefit policyholders. Conseco filed bankruptcy in 2002 due to losses in its consumer finance subsidiary, but its insurance companies continued to operate. If AIG's insurance subsidiaries are unable to continue operating following an AIG default, they could be seized by state regulators and put into rehabilitation.

It is possible that the failure of the AIG parent holding company could lead to additional losses at AIG's insurance subsidiaries. The intra-company exposures discussed above are one possible channel for this to occur. If an insurance company is found to be insolvent, its regulator may choose to liquidate it. In that event, a state guaranty fund will pay claims, up to a cap, and may provide for continuing coverage by transferring the policies to another insurance company.

Whether AIG's insurance subsidiaries are put into rehabilitation or whether they are liquidated, a potential systemic risk exists if the public loses confidence in insurance companies more broadly. For example, life insurance companies are vulnerable to a run by policyholders with cash value policies.

Direct credit exposures to AIG

On September 16, AIG reported that banks had $30 billion in exposure to it on various bank loan facilities and lines of credit, of which about $7 billion was to U.S. institutions. A more recent measure of direct credit exposure is not available.

Sarah Dahlgren/NY/FRS
11/09/2008 10:47 PM

To Marc Symons, chris mcshea, vincent.baldan@ey.com
cc
bcc
Subject busy day

it all came together....amazing to watch it happen over the course of the day

we have signed agreement on both sides for the preferred equity from UST.....

we are getting signed signature pages from the 8 counterparties to ML III...additional calls to be made to remaining counterparites with same offer....

we got approval from our board, from the FSOB/TARP, and from AIG's board....and various documents are being signed as we speak....

remaining outstanding stuff -- 10Q still needs to be fixed....our lawyers and DPW are going with the company to the printers to make sure this gets done......still aiming for the 6 a.m. release of the 10Q

still waiting for another turn on the Q&As from Rich Charlton....thanks for your feedback on that.....

likely to be a late night for folks on the 10Q front (mostly making sure that the ML II and ML III details get in there correctly)

as for me, I'm heading to my apartment to get some sleep.....have an 8 a.m. press briefing

and then I think I'm going to Disneyworld

:-)

see you tomorrow.....thanks for everything.....can't believe what's happened in just under eight weeks....seems like just yesterday......

and there's a long road ahead.....we're gonna need to get even more creative as we think about additional solutions and responses!.....

please share with your team.....this is a milestone on the journey (as Ed said a number of times this evening in the board meeting)......and we couldn't have done it without you and your team....

thanks

* * * * * * * * * * * * * *
Sarah Dahlgren
Senior Vice President
Federal Reserve Bank of New York
212-720-7537 (work)
917-770-8147 (blackberry)

visit www.newyorkfed.org
* * * * * * * * * * * * * *

Sandra Lee/NY/FRS

09/22/2008 09:16 PM

To: Steven J Manzari/NY/FRS@FRS

cc: Thomas Baxter/NY/FRS@FRS, Joyce Hansen/NY/FRS@FRS, HaeRan Kim/NY/FRS@FRS

bcc:

Subject: Fw: Call with AIG -FP

Steven,

Below is an e-mail summarizing the call David Aman (outside counsel from Cleary Gottleib) and I had with William Shirley of AIG Financial Products and his outside counsel about how pricing disputes are to be resolved as described in the confirmations governing AIG's CDS with Societe Generale.

Please let me know if you have any questions.

Regards,

Sandra Lee

----- Forwarded by Sandra Lee/NY/FRS on 09/22/2008 09:05 PM -----

"David Aman" <DAman@cgsh.com>

09/22/2008 08:26 PM

To: Sandra.Lee@ny.frb.org

cc:

Subject: Call with AIG -FP

Dear Sandra:

As you requested, the following is a brief summary of our conversation with Bill Shirley (of AIG Financial Products) and Jason Smith (of Weil Gotschal, AIG-FP's counsel).

* * *

<u>Legal Position:</u>

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On that call, Bill Shirley explained that their swap transactions (at least with SocGen) do not use the standard ISDA Credit Support Annex to determine "Exposure" with respect to a transaction; instead, the confirms override the CSA's "Exposure" definition and dispute resolution provisions, as shown on pp.8-9 of the attached confirm. "Exposure" is defined in the confirm based on a formula that uses the market value (undefined) of a particular Reference Obligation as its key input.

Unlike the CSA process I described, in the event of a dispute on one of these transactions, the valuation agent does not seek four mid-market bids. Instead, the parties jointly select a single Independent Dealer to fix the price for them. (If the parties can't agree on an Independent Dealer, each nominates one dealer and the two nominated dealers select the Independent Dealer.) The Independent Dealer then makes a binding determination of the market price of the Reference Obligation. There is no particular methodology stated for this determination.

In an illiquid market, an Independent Dealer asked to put a market value on an asset may very well attempt to estimate the price at which such asset may sell in the current market from a willing seller who owns the asset to a willing buyer. Since there are few buyers in today's market, this could result in a lower price by contrast with the standard CSA process under which mid-market bids are sought and averaged.

Status of SocGen transactions:

Bill explained that AIG-DP and SocGen are very far apart on the mark-to-market of the Reference Obligations (and therefore also the transactions). Apparently, however, neither party has yet sought the appointment of an Independent Dealer to resolve the questions. Instead, as is the common practice, they have been negotiating the marks in an attempt to reach a compromise. Bill did not seem to think he would get a good result if he pressed for an Independent Dealer -- he and Jason emphasized the difficulty of getting prices on over 30 sizeable transactions in this market.

*   *   *

I'm not sure there is anything more I can tell you, but please feel free to ask questions at any time.

Best regards,

David

David Aman
Cleary Gottlieb Steen & Hamilton LLP
One Liberty Plaza, New York NY 10006
t: +1 212 225 2262 | f: +1 212 225 3999
www.clearygottlieb.com | daman@cgsh.com

----- Forwarded by David Aman/NY/Cgsh on 09/22/2008 07:32 PM -----

William.Shirley@aigfpc.com

22 September 2008 06:14 PM

To
sandra.lee@ny.frb.org
cc
daman@cgsh.com, jason.smith@weil.com
Subject
SocGen Confirm

Sandra,

As requested, here is an example of the confirms governing our CDS with SocGen. The dispute provision in question is on pages 8 and 9. Speak to you momentarily.

Bill

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The information contained herein is being furnished for discussion purposes only and may be subject to completion or amendment through the delivery of additional documentation. This communication does not constitute an offer to sell or the solicitation of an offer to purchase any security, future or other financial instrument or product. The information contained herein (including historical prices or values) has been obtained from sources that we consider to be reliable; however, we make no representation as to, and accept no responsibility or liability for, the accuracy or completeness of the information contained herein. Such information is presented as of the date and, if applicable, time indicated. We do not accept any responsibility for updating any such information. Any projections, valuations and statistical analyses contained herein have been provided to assist the recipient in the evaluation of the matters described herein; such projections, valuations and analyses may be based on subjective assessments and assumptions and may utilize one among alternative methodologies that produce differing results; accordingly, such projections, valuations and statistical analyses are not to be viewed as facts and should not be relied upon as an accurate representation of future events.

Any market views or opinions expressed herein are those of the individual sender, except where such views or opinions are expressly attributed to our company or a named individual. Market views and opinions are current opinions only; we and the individual sender accept no responsibility to update such views and opinions or to notify the recipient when they have changed. We and our affiliates, officers, directors and employees may from time to time have long or short positions in, buy or sell (on a principal basis or otherwise), or act as market maker in, the securities, futures or other financial instruments or products mentioned herein. Subject to applicable law and notwithstanding anything that may be construed to the contrary, the recipient hereof and its employees, representatives, and other agents may disclose the U.S. federal income tax treatment and structure of any transactions described herein. We are not an advisor as to legal, taxation, accounting, regulatory or financial matters in any jurisdiction, and are not providing any advice as to any such matter to the recipient. The recipient should discuss such matters with the recipient's advisors or counsel and make an independent evaluation and judgment with respect to them.

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BFC Genesee SG CDS Confirmation (EX).pdf

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Memo to File

Date:	October 2, 2008
To:	Tom Baxter, Executive Vice President and General Counsel
From:	Sarah Dahlgren, Senior Vice President
Sub:	Request to engage BlackRock Solutions

In connection with the formation of Maiden Lane II and Maiden Lane III, (collectively, the "Entities"), the Federal Reserve Bank of New York (the "FRB-NY") requests the authorization to engage BlackRock Solutions ("BlackRock") to perform the following contemplated services:

1. Perform a fair value assessment and risk analysis on the AIG FP portfolio of CDS on CDO's transactions to be placed in Maiden Lane III.
2. Perform a fair value assessment and risk analysis on the portfolio of investments purchased in connection with the Securities Lending Program to be placed in Maiden Lane III.
3. Assist with the formation and structuring of the Entities.
4. Potentially become the asset manager of the Entities.

BlackRock is intimate with the details of the CDS on CDO's within AIG FP as a result of it being recently engaged by AIG to provide cash flow projections on a significant portion of the portfolio.

Additionally, BlackRock's Financial Markets Advisory Group is a world class leader in this field and has managed or advised on distressed structured finance portfolios totaling over $250 billion since mid-2007. BlackRock also worked with the FRB-NY on the $30 billion facility related to the JP Morgan/Bear Stearns merger, and currently works with many investment banks, insurers and global commercial banks.

BlackRock has been in discussions with AIG, Inc. to be engaged to perform services similar to those described above in items #1 and #2 above on AIG's behalf. To the best of our knowledge, BlackRock has not been engaged by AIG Inc. as of the preparation of this memorandum.

As a result of the word class organization, industry experience and familiarity with the portfolios contemplated for inclusion within the Entities, along with the need for the timely and efficient engagement of a service provider, our recommendation would be to engage BlackRock to perform the contemplated services.

Plan for AIG FP

Sarah Dahlgren

to:

deborah.bailey, Michael S Gibson, Mark VanDerWeide, Kieran Fallon, Rich Ashton, Jon.D.Greenlee

10/04/2008 01:54 PM

Cc:

Steven.Manzari, Clinton Lively, james.hennessy

Show Details

We required the firm to provide to us its plan to winddown AIG FP....working with McKinsey and Blackrock, the firm provided the attached late last night and we will be meeting with them on Monday to discuss further.... The firm at this point is unaware of the Maiden Lane structures that we are discussing (for obvious reasons), but those structures would be complimentary to what the firm is proposing for the rest of FP (you'll notice the "credit" block of the presentation on page 5 (number 5 business) is being taken care of by the "credit workout team".... If you'd like to discuss further after we've talked with the company on Monday, we can set something up for later in the day/evening..... holler if you have questions -- Clint Lively has been leading our efforts on FP.... thanks Sarah * * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * * * *

- AIG FP Restructuring Winddown Plan.pdf

Nova:
Overview of Structure Options

October 10, 2008

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BLACKROCK

Counterparty Concessions

The modeled structure assumes the counterparty receives par in exchange for the CDO

A counterparty concession would improve security / economics to FRBNY as well as to AIG

Counterparties should be willing to offer some concession:

- Have received $12.8 billion in collateral since FRBNY intervention on 9/16 (out of $30.2 billion total posted to-date)
- Under the proposed structure
  - Would receive a major infusion of liquidity, including additional $4.2 billion collateral requested
  - Would reduce risk-weighted assets on balance sheet (capital benefit)
- Benefitted generally from avoidance of systemic risk from AIG failure
- Are currently exposed to AIG credit risk on future declines in MTM value of CDOs

BRS modeled three concession methods:

1. **Flat Haircut:** Same haircut across all transactions / counterparties (i.e., 2 points on notional exposure)
2. **Credit Event-based:** Transfer price based on the following haircut method:
   - 50 bps concession / year until projected credit event under extreme stress scenario
   - Capped at 3 points with a minimum of 50 bps
   - Weighted average concession across the book is 1.6% -- thus transfer price would be 98.4
3. **Deep Concession:** as a function of collateral received up to close of ML III transaction - we assume a concession of *half* of received collateral so far (19 points total)

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Summary of Results at Varying Counterparty Concessions

Analysis Results at Varying Concessions

	At Par (previously shown)	Flat Haircut	Credit Event Based	Deep Concession
Concession from Counterparty (MM)	None	$1,338	$1,103	$6,400
Payment to Counterparty (MM)	$66,900	$65,562	$65,797	$60,500
Collateral Posted as of 10/31[1] (MM)	$34,396	$34,396	$34,396	$34,396
Size of Senior Note (MM)	$27,504	$26,166	$26,401	$21,104
Size of Equity (MM)	$5,000	$5,000	$5,000	$5,000
Residual cash flows (Debt % - Equity %)	67% - 33%	67% - 33%	67% - 33%	67% - 33%
Base Case Returns				
Senior Note IRR	16.4%	17.6%	17.4%	23.7%
Senior Note WAL	2.5	2.3	2.4	1.8
Senior Note Last Cashflow	Oct-2013	Jun-2013	Jul-2013	May-2012
Equity IRR	19.0%	20.0%	19.9%	24.5%

[1] $30.2 collateral posted as of 10/24; the analysis assumes $4.2bn in additional collateral posted from 10/24 to 10/31

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Concession Options by Counterparty

Counterparty	Exposure ($ MM)	Collateral Posted ($ MM) Sep 16	Collateral Posted ($ MM) Oct 24	Uncollateralized Balance ($ MM) Sep 16	Uncollateralized Balance ($ MM) Oct 24	Concessions: Flat Haircut ($ MM)	Flat Haircut (%)	Credit event-based ($ MM)	Credit event-based (%)	Deep Concession ($ MM)	Deep Concession (%)
Bank of America	776	207	267	569	508	16	2.0%	12	1.6%	30	3.9%
Bank of Montreal	1,372	199	308	1,174	1,065	27	2.0%	35	2.6%	54	4.0%
Barclays	2,383	928	1,293	1,455	1,090	48	2.0%	23	1.0%	183	7.7%
BGI (Cash Equivalent Fund II)	122	9	37	113	84	2	2.0%	1	0.8%	14	11.8%
Calyon	4,327	1,231	2,289	3,096	2,038	87	2.0%	65	1.5%	529	12.2%
Coral Purchasing (DZ Bank)	1,815	290	734	1,525	1,080	36	2.0%	33	1.8%	222	12.3%
Deutsche	7,638	621	2,823	7,017	4,815	153	2.0%	40	0.5%	1,101	14.4%
George Quay	89	0	0	89	89	2	2.0%	2	2.4%	0	0.0%
Goldman Sachs	14,539	6,050	7,834	8,489	6,705	291	2.0%	271	1.9%	892	6.1%
HSBC Bank	565	173	260	393	306	11	2.0%	3	0.5%	44	7.7%
LEAFS	844	0	0	844	844	17	2.0%	4	0.5%	0	0.0%
Merrill Lynch	6,377	1,975	3,135	4,401	3,241	128	2.0%	128	2.0%	580	9.1%
Mizuho Bank	1,769	0	0	1,769	1,769	35	2.0%	9	0.5%	0	0.0%
Orchid CDO	22	0	0	22	22	0	2.0%	1	2.9%	0	0.0%
Rabobank	1,131	52	636	1,079	495	23	2.0%	13	1.2%	292	25.8%
Remo Finance	400	0	0	400	400	8	2.0%	2	0.5%	0	0.0%
Royal Bank of Scotland	1,132	435	624	697	508	23	2.0%	25	2.2%	95	8.4%
Societe Generale	16,399	4,271	8,378	12,128	8,021	328	2.0%	322	2.0%	2,053	12.5%
STRIPS III	45	0	0	45	45	1	2.0%	0	0.5%	0	0.0%
UBS	4,218	931	1,457	3,287	2,761	84	2.0%	89	2.1%	263	6.2%
Wachovia	937	83	178	854	759	19	2.0%	24	2.6%	48	5.1%
Total	66,900	17,454	30,254	49,445	36,646	1,338	2.0%	1,103	1.6%	6,400	9.6%

James P Bergin/NY/FRS
11/03/2008 12:14 PM

To HaeRan Kim/NY/FRS@FRS, Joyce Hansen/NY/FRS@FRS
cc
bcc
Subject Fw: Question about terminations in the event of downgrade

Fyi. Alex is trying to figure out the terms of the CSAs so he can figure out how to price a concession. He's asked DPW to do some work on this.
----- Forwarded by James P Bergin/NY/FRS on 11/03/2008 12:08 PM -----

"Bjerke, Bjorn"
<bjorn.bjerke@dpw.com>
11/03/2008 12:02 PM

To <Alejandro.LaTorre@ny.frb.org>
cc <Paul.Whynott@ny.frb.org>, <James.Bergin@ny.frb.org>, "Anderson, Paul" <paul.anderson@dpw.com>
Subject RE: Question about terminations in the event of downgrade

Ok we will review and revert.
Best,
Bjorn

From: Alejandro.LaTorre@ny.frb.org [mailto:Alejandro.LaTorre@ny.frb.org]
Sent: Monday, November 03, 2008 11:41 AM
To: Bjerke, Bjorn
Cc: Paul.Whynott@ny.frb.org; James.Bergin@ny.frb.org
Subject: Question about terminations in the event of downgrade

We need a good understanding of the CSAs for the 6 largest CPs to AIG; at a minimum we want to know the following.

1. Are they all using standard CSAs or have they been calibrated to meet bilateral considerations?
2. What are the rules around valuation disputes?
3. What are the rules around terminations/closeouts in the event of downgrade (not just default).
4. What are the rules around min threshold posting amounts?

Have I missed anything?

On the last point, if AIG is downgraded to a certain threshold, I understand that counterparties have the right to terminate. Do we know whether this is true for all the CSAs for the counterparties? Also is it possible to argue that the economic costs of this form of termination would exceed what we are proposing (tearing up at some concession plus purchase of underlying CDO)? This might be a way at pricing the concession.

Bjorn, if you or someone at DPW know or can find out the answers to these already (you mention some of these issues in the memo to Terry), please advise. Any insight into what the CSAs state on this would be helpful as would your thoughts on whether the costs

Thanks

Issues:

1> Residual risks of AIG FP portfolio:
   a. Short protection on $270bil of bank loans on balance sheets of European banks (regulatory arbitrage trades)
      i. Bet is that the portfolio remains high quality through the next several years
   b. Investment Portfolio $45bil
   c. Highly structured derivative products portfolio
      i. $2tril notional
      ii. out to 40yr maturities
      iii. multi-factor option books
   d. MLIII should be structured to accept other trades at a later time (e.g. regulatory arbitrage trades) if necessary.

2> Key man risk in winding down AIGFP
   a. Flight of risk management talent required to execute an orderly unwind of a large, complex OTC derivative book.

3> Valuation of CDOS on transfer from AIGFP to Maiden Lane III
   a. Distressed sale price (new money in this market)
   b. Price underlying counterparty collateral calls
   c. Price underlying AIGFP collateral provision
   d. Price on AIG books.

4> Capital Structure and Returns of MLII and MLIII
   a. AIG first loss participation with limited upside;
   b. Cannot impair capital or liquidity position of AIG (contrary to intent);
   c. Transfer of risks and return to FRB leads to consolidation on FRB balance sheet.

5> Return of collateral constitutes a $33bil liquidity call on the financial system
   a. Some counterparties may have difficulty returning collateral;
   b. Perhaps incentive for concession on a tear-up price; or
   c. Failure to return creates loan from FRB – security to be determined.

6> Review implications of AIG realization of unrealized $33bil loss.

7> Urgency – in order to move quickly, we can guarantee performance on the trades initially and later novate them MLIII
   a. Guaranty conditional upon
      i. return of collateral
      ii. release of AIG guaranty
      iii. AIG guaranty to cease being a credit support document
      iv. AIG to cease being a credit support provider
      v. release of AIG downgrade triggers
      vi. seek other counterparty price concessions.

Notes on the CDS Portfolio:
- roughly 112 trades
- 16 counterparties account for 94% of the notional
- Notional value $78bil

"Singh, Shelley (IBD)" <Shelley.Singh@morganstanley.com>

10/19/2008 07:24 PM

To

<Paul.Whynott@ny.frb.org>, <Sarah.Dahlgren@ny.frb.org>, <Amy.Flynn@ny.frb.org>

cc

"Abbey, Jared (IBD)" <Jared.Abbey@morganstanley.com>, "Bischof, Eric (IBD)" <Eric.Bischof@morganstanley.com> <Peter.Juhas@morganstanley.com>, "Angelova-Makki, Anna (IBD)" <Anna.Angelova-Makki@morganstanley.com>, "]

Subject

RE: Materials for 5pm Capital Structure discussion

All, Please find attached the revised materials that were discussed on the 5 pm call. We will send out another updated version tomorrow with the additional requests. Best, Shelley **Shelley Singh** Morgan Stanley | Investment Banking Division 1585 Broadway Floor 31 New York, NY 10036 Phone: +1 212 761-3736 Fax: +1 646 225-5351 Shelley.Singh@morganstanley.com [illegible] PLEASE CONSIDER OUR ENVIRONMENT BEFORE PRINTING THIS E-MAIL. **From:** Singh, Shelley (IBD) **Sent:** Sunday, October 19, 2008 4:50 PM **To:** Paul.Whynott@ny.frb.org; Sarah.Dahlgren@ny.frb.org; Amy.Flynn@ny.frb.org **Cc:** Abbey, Jared (IBD); Bischof, Eric (IBD); Doak, Michael (IBD); Juhas, Peter (IBD); Angelova-Makki, Anna (IBD) **Subject:** Materials for 5pm Capital Structure discussion All, Please find attached the materials for the 5 pm call. ACCESS CODE Participant Code: 542885 DIAL-IN INSTRUCTIONS MS Internal Ext: 000-1313 NA Access: +1 718 754-6999 / 914 225-6999 EU Access: +44 20 7425-2721 / 7677-2721 ASIA Access: +81 3 5424-5253 / 6401-5253 Toll free- NA: 1 877 777-8895 Toll free- Non-NA: Intl dial code + 80 07 770-0000 Best, Shelley *Privileged All information contained in this email message, including any attachments thereto, shall not be disclosed outside the Federal Reserve System or the U.S. Government, consistent with the Freedom of Information Act (5 U.S.C. 552). Information being delivered to the Federal Reserve Bank of New York by Morgan Stanley, as a contractor and paid consultant to the Federal Reserve Bank of New York, is for the exclusive use by Federal Reserve Bank of New York in its deliberative process antecedent to its adoption of an internal decision. Morgan Stanley has no interest or stake in the outcome of that decision-making process. Information delivered by the Federal Reserve Bank of New York to Morgan Stanley remains under the control of the Federal Reserve Bank of New York and is part of its deliberative process* **Shelley Singh** Morgan Stanley | Investment Banking Division 1585 Broadway | Floor 31 New York, NY 10036 Phone: +1 212 761-3736 Fax: +1 646 225-5351 Shelley.Singh@morganstanley.com BE CARBON CONSCIOUS. PLEASE CONSIDER OUR ENVIRONMENT BEFORE PRINTING THIS E-MAIL. [illegible]

- 2008.10.19 Capital Structure v2.pdf

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RE: Materials for 5pm Capital Structure discussion 000000000003FFFF006E001372080000

Sarah Dahlgren

Singh, Shelley (IBD)

10/20/2008 10:25 AM

Cc

Amy.Flynn, "Angelova-Makki, Anna (IBD)", "Bischof, Eric (IBD)", "Head, James (IBD)", "Abbey, Jared (IBD)", "Doak, Michael (IBD)", Paul.Whynott, "Juhas, Peter (IBD)", Steven.Manzari, Amy.Flynn, Marc.Symons, chris.mcshea, ethan.james, marshall.huebner

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I got some early feedback from Tim...he's good with the direction in which this is heading....I'm going to send the next version to Warsh and Jester..... one additional variant that he'd like to add/consider -- giving up some of the upside in the trust....so, if we are going to subordinate any part of the loan, he'd like to also see what we'd recommend in terms of raising equity now by the firm -- and exchanging for shares in the trust (2 common raised for one share in the trust or something like that). . timing on the equity raise, dollar amount to raise, amount to come out of the trust (in what form, etc. .), what the capital structure would look like, how this might help with the subordination issue (so, can we actually get some paid down and not have to subordinate, etc...) is this enough clarity to run with? .if not, happy to brainstorm further..... thanks! Sarah * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * *

Fw: FP Downgrade Impact

lawrence.prybyls
ki

Catherine.Voigts, Clinton.Lively

10/23/2008 08:01 PM

Cc

Marc.Symons, Steven.Manzari, Sarah.Dahlgren

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491

History: This message has been forwarded.

Cathy and Clint - I spoke with Elias about the FP downgrade impact analysis - collateral postings and terminations. He walked me through the attached memo (he said that he shared with Sarah earlier today). In addition to the memo, we discussed the following: Non-GIC portfolio - (i.e. the derivatives outside the CDS books) have an additional termination cost estimated to be $100 to $200 million. The $2 billion / $2.8 billion referenced in the attachment reflects FP's mid market. Multi-Sector CDS - If you used the GS tear up discussions (althought they only a subset of deals and largely those closer to events of default) to estimate a replacement cost and then extrapolate to the entire portfolio. the replacement cost estimate would be $8 billion upon termination. No one really has a good handle on these figures givne market situation. We also discussed that dispute procedures upon termination are more limited than is a standard collateral dispute. He also felt that GS would be the counterparty most likely to terminate given the other counterparties appear to be holding the bonds. Assuming that the 2a7 positions under repo are the Project Max positions, this is about a $5 billion liquidity impact (cathy - can you confirm). Corporate Arb - Liquidity impact assuming all the collateral calls and half the notional terminates with a replacement cost equal to 20% of the market value would be $980 million. Elias said that Jon Liebergal and Christian Pezeu (Christian.Pezeu@aig.com / 212 770 6991) are working on this for him and they can give us the detail/support. Christian is the point guy. He also noted that a comprehensive legal legal review is under way to validate the provisions and this will not be finalized until early next week - so things are subject to change. Cathy - Jon and Christian will be in Wilton tomorrow. I am not sure of your plans for tomorrow. Once we review the figures we can summarize in a table for everyone with more details on assumptions, etc. Hank

Ernst & Young ®
Ernst & Young LLP
Hank Prybylski Financial Services

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----- Forwarded by Lawrence Prybylski/NewYork/AUDIT/EYLLP/US on 10/23/2008 07:22 PM -----

"Habayeb, Elias" <Elias.Habayeb@aig.com>

10/23/2008 07:07 PM

To
"lawrence.prybylski@ey.com" <lawrence.prybylski@ey.com>
cc

Subject
Rating Agency Talking Points.doc

 - Rating Agency Talking Points.doc

492

RE: Further update 000000000003FFFF006E001372080000

Sarah Dahlgren

Wiedman, Mark

10/24/2008 12:35 PM

Cc

steven manzari

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just talked with Herzog.... he will get on the collateral centralization issue....he also told me that Goldman couldn't give them prices.... * * * * * * * * * * * * * * *Sarah DahlgrenSenior Vice PresidentFederal Reserve Bank of New York212-720-7537 (work)917-770-8147 (blackberry)visit www.newyorkfed.org* * * * * * * * * * * * * * *

"Wiedman, Mark" <Mark.Wiedman@blackrock.com>

10/24/2008 12:33 PM

To

<steven.manzari@ny.frb.org>, <sarah.dahlgren@ny.frb.org>

cc

Subject

RE: Further update

More info to come -- lots of confusion -- GS says "we need more time" . . .

From: Wiedman, Mark **Sent:** Friday, October 24, 2008 12:28 PM **To:** Steven Manzari (steven.manzari@ny.frb.org); 'Sarah J. Dahlgren (sarah.dahlgren@ny.frb.org)' **Subject:**

Fw: Materials for 4pm meeting on ML III

HaeRan Kim

Steven J Manzari, Paul Whynott, Sarah Dahlgren, Jim Mahoney

10/26/2008 04:52 PM

Cc:

Joyce Hansen

Show Details

Are we planning on talking to dealers about tear-ups before or after we get indication that the Board will approve a 13(3) loan?

----- Forwarded by HaeRan Kim/NY/FRS on 10/26/2008 04:43 PM -----

Amy Flynn/NY/FRS

10/26/2008 03:43 PM

To
HaeRan Kim/NY/FRS@FRS
cc
James Hennessy/NY/FRS@FRS, Joyce Hansen/NY/FRS@NY
Subject
Re: Materials for 4pm meeting on ML III

Yes, please. I've included the call-in below.

Conference bridge information:
Toll Free Dial in Number: **888-557-8511**
Int'l Access/Caller Paid #: 215-446-3649
Access code: **3678482#**

* * *
Amy Flynn
Federal Reserve Bank of New York
Office: 212-720-6431
Cell: 347-266-4820

HaeRan Kim/NY/FRS

10/26/2008 03:41 PM

To: Amy Flynn/NY/FRS@FRS

cc: James Hennessy/NY/FRS@FRS, Joyce Hansen/NY/FRS@NY

Subject: Re: Materials for 4pm meeting on ML III

I'm at home. Do you want me to call in?

Sent from my BlackBerry Handheld.

----- Original Message -----
From: Amy Flynn
Sent: 10/26/2008 03:36 PM EDT
To: HaeRan Kim
Cc: James Hennessy
Subject: Fw: Materials for 4pm meeting on ML III

Hi HaeRan,

We are having a 4pm meeting with Tim Geithner today to discuss issues around the ML III structure. Do you think you would be able to attend the meeting? We'll be gathering in one of the conference rooms on 13th floor. The materials for the meeting are included in the email below.

Thanks, --Amy

***
Amy Flynn
Federal Reserve Bank of New York
Office: 212-720-6431
Cell: 347-266-4820

----- Forwarded by Amy Flynn/NY/FRS on 10/26/2008 03:30 PM -----

Amy Flynn/NY/FRS

10/26/2008 03:34 PM

To: Timothy Geithner/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS, Terrence Checki/NY/FRS@FRS, Christine Cumming/NY/FRS@FRS, Michael Silva/NY/FRS@FRS, Meg McConnell/NY/FRS@FRS, Paul Whynott/NY/FRS@FRS, Jim Mahoney/NY/FRS@FRS, Steven.Manzari@ny.frb.org, Amy Flynn/NY/FRS@FRS

cc:

Subject: Materials for 4pm meeting on ML III

Please find attached materials for the 4pm meeting to discuss Maiden Lane III.

[attachment "Slides for MS on MLIII 10-26-08.ppt" deleted by HaeRan Kim/NY/FRS]

[attachment "2008-10-25 MLNE III Structure v2.ppt" deleted by HaeRan Kim/NY/FRS]

***
Amy Flynn
Federal Reserve Bank of New York
Office: 212-720-6431
Cell: 347-266-4820

Further update It appears that GS didn't come back with #'s to tear up, which puts AIG's inability to tear up swaps in a different light. Update to come. It looks like NO ONE wants to take on additional risk. Being paranoid, I suspect they may also sniff a Fed solution in the background.

496

FYI 000000000C003FFFF006E001372080000

Paul Whynott

t
o
:
Skip.Curth

10/27/2008 01:40 PM

Cc
joe.palumbo, lawrence.prybylski, "Richard Gonseth", Alejandro LaTorre, Danielle Vicente, Steven J Manzari, Jim Mahoney

Show Details

Alex and I spoke briefly with Stacey at BlackRock, in essentially priority order.

They are working on the concession analysis, leveraging Zach and Nagy (sp?).
She is taking the lead on their end putting together the deal book. Looking to put together a deck that we can then use for the Board Staff briefing and use the executive summary for the Board of Governors. It's completeness depends a bit on when the numbers flow in to her, but she anticipates being able to circulate at the end of day (BlackRock end of day) today.
BlackRock is also working to develop the new scenarios by counterparty.
We reminded them of the need to do the analysis on the securities that may be pledged to support AIG's junior note.

Stacey will send who will work on what steps for BlackRock for the project plan and will develop out the steps for the plan where she can. She will also indicate where she feel BlackRock is the lead v. a participant

Paul

Paul Whynott
Federal Reserve Bank of New York
Work (212) 720-2388
Cell (914) 715-9886
Berry (917) 254-6896

Michael S Gibson/Board/FRS@BOARD
Sent by: Michael S Gibson/BOARD/FRS@BOARD

10/31/2008 02:41 PM

To
Sarah Dahlgren/NY/FRS@FRS

cc
Deborah P Bailey/BOARD/FRS@BOARD, Jon D Greenlee/BOARD/FRS@BOARD, Kieran Fallon/BOARD/FRS@BOARD, Paul Whynott/NY/FRS@NY, Rich Ashton/BOARD/FRS@BOARD, Steven J Manzari/NY/FRS@FRS, Clinton Lively/NY/FRS@FRS, Jim Mahoney/NY/FRS@FRS, Michael S Gibson/BOARD/FRS@BOARD, Scott Alvarez/BOARD/FRS@BOARD

Subject
AIG questions from our meeting with Govs. Kohn and Warsh

Sarah,

We met with Govs. Kohn and Warsh today to update them on the package of measures being prepared for AIG.

The governors asked two questions in the meeting that we did not know the answers to. I expect these are issues that someone on your team is already working on, but we would like to get the latest information from you so we can get back to the governors with answers.

1. Who is overseeing the tear-up process on the CDS? There are two issues here, concessions and Goldman.

Concessions: the worry is that giving the counterparties par in exchange for the underlying CDO security might be giving them a gift - they no longer have AIG credit risk, and whatever CVA they have taken against potential future exposure to AIG will be released upon tear-up. If a counterparty has not received all the collateral it has called for, the tear-up eliminates current exposure also. On the other hand, AIG is now receiving government support so the perceived credit risk of AIG is less. Also, AIG needs to get the CDS torn up to put its problems behind it, so its bargaining power may be weak. If I understand the current version of the proposed structure, any concessions will result in an excess amount left in the escrow account which pays down the Fed's senior note. This may reduce AIG's incentive to bargain for the best concession possible. Is Morgan Stanley or some advisor from our side embedded in the tear-up negotiations to track these issues?

Goldman: is a special case because their CDS with AIG are a naked short position and they don't own the bonds. If the CDS are just torn up at current mark-to-market, the value of that mark influences the cash Goldman will receive in a way that is not the case for the counterparties who own the bonds and will be receiving par. The Fed, Goldman's senior management, and Treasury all have an interest in making sure the negotiation of the mark between AIG and Goldman is done in a fair way. However, the normal procedure might be for the negotiations to be done between someone at AIGFP and their counterpart on a trading desk at Goldman. A Goldman trader may not share the perspective of Goldman's senior management and may attach higher value to an extra billion dollars of P&L that could affect his or her 2008 bonus, even if that carries significant reputation risk for Goldman as a firm. Again, is Morgan Stanley or some advisor involved here and aware of the issue? Is there a contingency plan to approach Goldman at a more senior level if roadblocks start appearing in the negotiations?

2. What public disclosures will be made of the mark-to-market on ML II and ML III once they are consolidated on FRBNY's balance sheet?

The governors were concerned that the market could attach a disproportionate significance to any public disclosure of "the Fed's" marks on the nonagency RMBS and ABS CDO portfolios once ML II and ML III are consolidated onto FRBNY's balance sheet. Do we have a strategy for that? Would the disclosure be the same as Maiden Lane LLC (quarterly disclosure of fair value of the holdings of ML II and ML III on the H.4.1)?

Three more questions that are mine, not the governors.

1. Given all the public hue and cry about the transit authorities whose tax-motivated lease transactions are in danger of unwinding due to AIG's downgrade below AAA, are there other similar transactions that we should know about (and alert the governors about)? I assume this transaction was part of the AIGFP TDG portfolio; do what know what else lurks there?

2. What is the status of the FP winddown?

3. Can we have an update on the asset disposal process?

Thanks,
Mike

CONFIDENTIAL FRBNY-TOWNS-R1-113012

Re: AIG questions from our meeting with Govs. Kohn and Warsh 000000000003FFFF006E001372080000

Alejandro LaTorre

t
o
:

Steven J Manzari, Paul Whynott, Clinton Lively, Jonathan Polk, Jim Mahoney

11/02/2008 09:33 AM

Cc

Sarah Dahlgren

Show Details

Paul/jim

Can take a first crack for your comments. Let's discuss when we meet later today - I should be in around noon

Alex Latorre
Federal Reserve Bank of New York
Office: 212-720-2728
Cell: 917-916-0760

Sent from my BlackBerry Handheld

----- Original Message -----
From: Steven J Manzari
Sent: 11/01/2008 09:32 PM EDT
To: Paul Whynott; Alejandro LaTorre; Clinton Lively; Jonathan Polk; Jim Mahoney
Cc: Sarah Dahlgren
Subject: Fw: AIG questions from our meeting with Govs. Kohn and Warsh

Paul, Alex, Jim, - can you draft a response to Mike on # 1 and 2.
Clint, JP, can you draft a response to Mike on 3-5 (Mike's 1-3).
Tx,
Steve

Steven J. Manzari
Federal Reserve Bank of New York
33 Liberty Street
New York, NY 10045
T 212 720 5881
F 212 720 7922
C 646 701 4635
24 HR FRBNY CENTRAL WATCH 212 720 2222
----- Forwarded by Steven J Manzari/NY/FRS on 11/01/2008 09:29 PM -----

RE: CDS Solutions

Bjerke, Bjorn

t
o
:

Paul.Whynott

11/02/2008 09:51 PM

cc:

Terrence.Checki, Alejandro.LaTorre, Steven.Manzari,
"Anderson, Paul"

Show Details

Terry,

This is to follow up on our discussions on whether AIG FP would be likely to receive back collateral posted with respect to its exposure under a credit default swap (a "CDS") with a counterparty if ML III were to make an offer to such counterparty to purchase the relevant collateralized debt obligation (the "CDO") that is the reference obligation for such CDS coupled with an offer to also pay a tear-up price for the CDS. For reasons explained below, I will assume that the same offer would be made to any reference dealer that has entered into a replacement transaction with the counterparty in connection with a

termination of the CDS.
The short answer is: Possibly, if ML III's offer as a business matter causes improved market quotes in connection with the CDS.
As a result of the dispute resolution mechanism in the ISDA credit support annex, the key question in this analysis is whether as a business matter all the relevant reference dealers would be willing to take ML III's offer into account if and when they quote a price to enter into a replacement transaction with the counterparty. Traders are not obligated to take that offer into account when providing their quotes and thus unless you receive an "of course" from each trader when asked whether it would give, and continue to give, a quote that takes ML III's offer into account, this is a far from certain proposition. Set forth below is an argument that would permit the relevant dealers to agree to take ML III's offer into account but this would be an unusual set of facts and that we cannot predict how the market would react to it nor can we be entirely confident about the legal outcome.
Also worth noting is that this return of collateral, as a result of FRB's constraints on lending, may not resolve AIG FP's liquidity issues because the returned collateral should be placed in escrow with ML III for use by that entity in case its offer is accepted. It is also possible that the offer does not solve AIG FP's exposure to fluctuations in market prices of CDOs. This would be the case, for instance, if the FRB requires AIG FP to pay any difference between market price of the CDO on the offer date compared to the purchase date and to secure that obligation by posting additional collateral to ML III. Finally, the offer should be "real" and set at a price with a reasonable likelihood of being accepted by counterparties and reference dealers so as to reduce risks of arguments that the offer is designed not to be real but simply a some form of interference or manipulation designed only to force return of collateral.
Consequently, given these uncertainties and the additional concerns outlined below, an offer by ML III as described above might have benefits for the negotiations among ML III, AIG FP and the reference dealers but may not necessarily be suitable as a longer term solution for AIG FP's liquidity issues and the efforts to insulate AIG from further decline in CDO market values. I would also recommend that we follow up with MS or other economic advisers (or that you separately follow up with traders directly) to get their view of whether the traders would likely take ML III's offer into account for purposes of providing quotations.

Analysis:

The standard provisions of the ISDA credit support annex (the "CSA") dictate that the amount of additional collateral to be posted (or excess collateral to be returned) shall be determined by the Valuation Agent. According to the standard CSA terms, the Valuation Agent is the party receiving a transfer of additional collateral or return of excess collateral as the case may be. This means that if there is a large discrepancy between two parties in how they value the exposure, the right to calculate the collateral posting requirement could shift each time an additional posting or a return of collateral has been made. The CSA keys its collateral posting requirement of what the termination amount payable would be if the relevant calculation date were a Termination Date under the ISDA. In a dysfunctional market we can assume that this calculation will be made pursuant to the "loss" method which applies if either the parties have elected "loss" or if "market quotation" applies but fewer than 3 reference dealers provide quotes.

Since AIG FP is the party with a current posting requirement, the relevant loss calculation would be a determination of what losses counterparty would incur if the CDS terminates as a result of an event of default for which AIG FP is the defaulting party. If AIG FP demands a return of excess collateral, then AIG FP is the valuation agent for the return amount that would determine counterparty's loss amount. AIG FP could reasonably point to ML III's offer and substantiate that if the CDS with AIG FP were to terminate, then counterparty could transfer the CDO to ML III (together with proof that the CDS has terminated) for a payment of ML III's offer. Since AIG FP's obligation under the CDS is for payment of par for the CDO in return of a transfer of the CDO to AIG FP, counterparty would be made whole if it were to enter into the cover transaction with ML III and seek payment of the shortfall amount from AIG FP. (This amount would be further adjusted to account for the protection premiums that counterparty saved but I will ignore those payments for purposes of this discussion).

The point in the preceding paragraph can be illustrated with a numeric example. Say that the CDO had a par value of $100 and that ML III's offer to purchase the CDO in conjunction with a termination of the CDS was $95. In that case, the shortfall that ML III would have to pay after the counterparty has availed itself of the loss mitigation offered by ML III would be $5 and therefore AIG FP could reasonably argue that counterparty's exposure to AIG FP is $5.

However, the counterparty could avail itself of the CSA's dispute mechanism. The CSA specifies that in the case of a dispute, the parties shall transfer the undisputed amount and then market quotes shall be sought from four dealers for the mid market price of how much they would pay, or require to be paid, as the case may be to enter into a transaction with counterparty that has the effect of preserving the economic position of counterparty if the CDS with AIG FP were to be terminated. If at least one dealer delivers a quote, then that quote becomes the exposure (and if more than one dealer provides a quote, the exposure is the average of such quotes). If no dealers deliver a quote, then the exposure shall remain as calculated by the relevant valuation agent.

A reference dealer is not required to consider ML III's offer in determining the offer price for a replacement transaction, but there is an economic argument to be made for why, as a business matter, they would be justified in so doing as illustrated by the following example:

Lets assume that:

Relevant Transaction: CDS on CDO between AIG FP as seller of protection and Counterparty as buyer of protection.

Reference Obligation: $100 par value of CDO.
Current market value of CDO: $60.
Exposure: $40 (par value - $60)
Collateral posting requirement: 105% of Exposure

Amount of collateral posted by AIG FP: $42

As a point of departure, AIG FP would calculate the Counterparty's loss in light of ML III's offer and, on that basis, substantiate an exposure of $5 and demand return of collateral posted in excess of 105% of such exposure. Should AIG FP's calculation stand, Counterparty would therefore be obligated to return $36.75 of Collateral.

If counterparty invokes its dispute rights and seeks 4 dealer quotes for a replacement transaction and at least one quote is given, then that quote would determine how much would be returned to AIG FP. One could argue with such reference dealers that it would make economic sense for them to take into consideration ML III's offer when providing a quote because the reference dealer could (1) enter into a replacement agreement for an up-front payment to it at its quoted price (2) negotiate a tear-up with counterparty of such replacement transaction combined with delivery of the CDO at above par, and (3) sell the CDO to ML III. The up-front payment that the dealer would have to receive in connection with entering into a replacement transaction would be equal to the sum of (x) the difference between what the reference dealer would have to pay to counterparty in step (2) and what such reference dealer would receive from ML III in step (3) and (y) the profit that the reference dealer would require. Thus, ML III's offer could cause the reference dealer to provide a quote for the replacement transaction in step (1) that rationally would be well below what the dealer otherwise would be willing to quote and thus, if that argument is accepted by the reference dealers, would reduce the exposure amount.
To illustrate this with a numeric example, lets assume the values and postings outlined above and in addition lets assume that the reference dealer is relatively confident that counterparty would accept a payment of $101 in combined payment for tearing up a CDS replacement agreement, and selling the CDO to, such reference dealer. Let's also assume that the reference dealer would demand a profit of $3 to enter into the replacement transaction, effectuating the tear-up and transferring the CDO to ML III. On that basis it would be rational for the reference dealer to demand an up-front payment of $9 to enter into a replacement transaction with counterparty. That $9 payment, when combined with the $95 that would be paid by ML III, equals $104 which is enough to pay $101 to counterparty for the tear-up of the CDS and sale of the CDO and to leave $3 for the reference dealer.
AIG FP's posting requirement would now be 105% of the $9 mark ($9.45) resulting in Collateral equal to $31.55 being returned to it from Counterparty.
Now, if some reference dealers provide quotes in agreement with the argument and others do not, then the exposure calculation would be the average of two sets of very different calculations, but is still likely to be substantially less than the current amount. On the other hand, the argument is complicated and unless the reference dealers agree, it is far from certain that they will take ML III's offer into account. If they get so uncertain of the economic reality that they don't provide quotes, then AIG FP's loss calculation would stand, but that result could be scuttled by a single reference dealer deciding to quote only on the basis of the expected internal CDO recovery amount. That uncertainty is somewhat enhanced by the fact that the very reference

dealers from which the quotations would be asked are likely to be counterparties to AIG FP to whom collateral under different but similar CDSs are posted and that therefore may take this impact on themselves into account when deciding whether to consider ML III's offer in connection with providing quotes.
If reference dealers either were to provide no quote or provide quotes that take into consideration ML III's offer then counterparties would likely have to return a significant amount of collateral posted by AIG FP. Such return amount reduced the counterparties ability to make money off of ML III's collateral postings and therefore increases their incentives to find a more permanent solution that provides the counterparties with more liquidity. The counterparties are likely to have better incentives still to enter into a permanent solution with ML III if ML III's offer is rescindable at any time (say upon 2 days notice) since counterparties would face the risk of AIG FP being able to post a significant amount of collateral on short notice if the ML III offer were rescinded.

Other Potential Issues

In addition to the key business issue of whether the reference dealers would agree to include ML III's offer as a consideration when providing their market quotes, there are also other important issues to consider and that maybe tilt the strategy toward one of a strategic play in connection with negotiating with counterparties rather than a stand-alone long term solution:

a. The strategy would not take the CDS of AIG FP's books (and would not terminate the tie to the Parent's guarantee). This means that the message provided by the "cleansing" strategy would become more muddled to investors and rating agencies.
b. If the CDS with the counterparty is not torn up and either a credit event or a termination event (in many cases a further downgrade of AIG FP would suffice) then the full par amount would be payable by AIG FP to the counterparty.
c. If AIG FP were to take a reference dealer up on an offer to novate, the total payments would likely be greater than par (because the relevant third party would need to turn a profit and the counterparty could demand a payment above par to terminate the replacement transaction and transfer the CDO such that the reference dealer could take advantage of ML III's offer). If the reference dealers recognize this, then they might either decide not to give a quote (which would be ok) or ignore ML III's offer as not likely to result in an actual trade and instead provide a quotation based on the CDO's recovery amounts more generally.
d. In order to avoid ML III being exposed to AIG's credit risk, all collateral returned to AIG FP would have to be returned to, and be held in, an escrow account for the benefit of ML III such that if ML III would have to make good on its offer, the FRB would not also pay AIG FP's share.
e. While economically it would be the same whether a CDO purchased by ML III on day one for 70 (combined with a payment by AIG FP of $25 for a tear up) declined to $60 on day 10 after such purchase, or whether a firm offer for the purchase and tear-up for $95 was made on day 1 and

the CDO was purchased for $70 on day 10 (with $25 still payable by AIG FP for the tear-up), the former seems more in line with FRB's policy of lending against value compared to the latter. AIG FP could be made to transfer to ML III additional collateral to compensate for such decline in CDO value, but such transfer obligation would result in AIG FP not being isolated from mark to market price movements in CDOs.

f. ML III would also have to be conscious of potential claims for market manipulation and tortuous interference with contract. If ML III's offer is real at a price with a reasonable possibility of being accepted by counterparties or reference dealers, then those concerns seem less founded. On the other hand, if ML III makes an offer that at a price not intended to be real but rather set at a level that is purposefully too low to be acceptable but instead aimed at just causing collateral to be returned from counterparties, then such concerns would be more worrisome. Consequently, it seems that the offer to purchase should be viewed as an interim step in conjunction with negotiating the tear-up and purchase price and not a permanent solution.

All the best,
Bjorn

From: Paul.Whynott@ny.frb.org [mailto:Paul.Whynott@ny.frb.org]
Sent: Friday, October 31, 2008 10:57 AM
To: Bjerke, Bjorn
Cc: Terrence.Checki@ny.frb.org; Alejandro.LaTorre@ny.frb.org; Steven.Manzari@ny.frb.org; Paul.Whynott@ny.frb.org
Subject: CDS Solutions

Bjorn,

Thank you for continuing to opine on the option Terry proposed yesterday to approach the CDS issue. In the interest of time and ensuring a direct channel of communication, would you give a call to Terry Checki to continue the discussion and your assessment of the potential pros and cons for this strategy? We are certainly happy to participate in any discussions, but recognize it may be most expedient for you to have a bilateral discussion.

Attached below is the contact information and Terry's e-mail address is in the cc line.

Terry Checki
Office: (212) 720-6740
Mobile: (917) 697-8690
Bjorn Bjerke, DPW
Office: (212) 450-4006
Mobile: (203) 249-3052

Regards,
Paul

Paul Whynott
Federal Reserve Bank of New York
Work (212) 720-2388
Cell (914) 715-9886
Berry (917) 254-6896

FRBNY DRAFT 11/04/08

Federal Reserve Bank of New York
[address]

[American International Group, Inc.
address]

Confidentiality Agreement

Ladies and Gentlemen:

Representatives of the party named on the signature page hereof (the "Counterparty") may be involved in communications with representatives of the Federal Reserve Bank of New York ("FRBNY")[, American International Group, Inc. ("AIG")], or an affiliate or subsidiary thereof, regarding the termination or potential termination of credit default swap transactions between the Counterparty or an affiliate or subsidiary thereof and AIG or an affiliate or subsidiary thereof, or the purchase or potential purchase of debt securities related to such transactions by an entity referred to as "Maiden Lane III LLC", FRBNY or an affiliate or subsidiary thereof (the "Proposed Transactions").

In connection with communications regarding the Proposed Transactions, Counterparty will receive certain information that is either nonpublic, confidential, or proprietary in nature. Such information may be received from FRBNY, AIG or their respective affiliates, subsidiaries, agents, advisors or employees (each, a "Disclosing Party") and may be provided in writing, orally, electronically or otherwise. Such information, in whole or in part, together with any documents that contain or otherwise reflect, or are derived from, such information, is hereinafter referred to as the "Information".

In consideration of engaging in discussions regarding the Proposed Transactions and receiving Information, Counterparty agrees as follows:

1. The Information will be kept strictly confidential in accordance with the provisions of this agreement and shall not, without the prior written consent of FRBNY, be disclosed by Counterparty, its agents, affiliates, advisors or employees, in any manner whatsoever, in whole or in part, or used by Counterparty, its agents, affiliates, advisors or employees, other than in connection with a Proposed Transaction involving Counterparty. Moreover, Counterparty agrees to transmit the Information only to its agents, affiliates, advisors and employees who are directly involved in, or necessary to Counterparty in effecting, Proposed Transactions in which Counterparty is involved; provided that any such person, prior to having any Information disclosed to them, shall be informed by Counterparty of the confidential nature of the Information and shall agree to be bound by the terms of this agreement. Counterparty shall be responsible for any breach of this agreement by its agents, affiliates, advisors or employees.

2. In the event that Counterparty or anyone to whom Counterparty transmits the Information pursuant to this agreement becomes legally compelled to disclose any of the Information, Counterparty will, if legally permitted, provide FRBNY with prompt notice thereof so FRBNY may seek a protective order or other appropriate remedy and/or waive compliance with the provisions of this agreement. Counterparty will furnish only the portion of the Information that is legally required. Notwithstanding the foregoing or anything herein to the contrary, Counterparty may, if required during the course of an audit or review by any governmental, regulatory or self-regulatory agency or authority having jurisdiction over Counterparty, disclose Information without notice to or consent from any Disclosing Party without causing a breach of this Agreement; provided that Counterparty shall notify FRBNY of such disclosure as soon as practicable and to the extent permitted by such agency or authority.

3. The term "Information" does not include information that (a) becomes generally available to the public other than as a result of a confidential disclosure by a Disclosing Party or anyone bound by a fiduciary obligation to a Disclosing Party or to whom a Disclosing Party confidentially transmitted the information or (b) was available to Counterparty on a non-confidential basis from a source other than a Disclosing Party, who, to Counterparty's knowledge, is not bound by a fiduciary obligation or confidentiality agreement with a Disclosing Party.

4. Counterparty will keep the fact of its receipt of the Information confidential and will not disclose such fact to any person, including its employees, not directly involved in, or necessary to Counterparty in effecting, the Transactions.

5. Counterparty agrees that if it or any of its agents or employees breach any of the limitations on disclosure or use or retention of Information set forth in this agreement, the FRBNY and AIG, or an affiliate or subsidiary thereof, are likely to suffer irreparable harm and, accordingly, that in addition to any other remedies available to FRBNY [and AIG] for such breach or a threatened breach, including the recovery of damages, FRBNY [and AIG] shall be entitled to an injunction restraining Counterparty and its agents and employees from any unauthorized disclosure or use, in whole or in part, of such Information.

6. In the event of litigation relating to this agreement, if a court of competent jurisdiction determines in a final, nonappealable order that a party has breached this agreement, then such party shall be liable and shall pay to the non-breaching party the reasonable legal fees such non-breaching party has incurred in connection with such litigation, including any appeal therefrom.

7. Counterparty understands that FRBNY [and AIG] will rely on Counterparty's agreements herein in engaging in discussions regarding the Proposed Transactions. The covenants, agreements, terms and provisions of this agreement shall bind the respective officers, employees, agents, affiliates, successors and assigns of the parties hereto; provided, however, that Counterparty may not assign any of its rights, duties, liabilities or obligations hereunder.

8. This agreement and the various covenants, agreements, terms and provisions, and the performance thereof, shall be construed, enforced and determined under and with reference to the laws of the State of New York. Counterparty hereby (i) consents to the exclusive jurisdiction of the courts of the United States for the Southern District of New York, and appellate courts thereof, with respect to any legal action or proceeding relating to this agreement or for recognition and enforcement of any judgment in respect thereof, (ii) waives any contention that any such court is an improper venue for such enforcement, and (iii) consents to service of process under the New York long-arm statute then in effect, including without limitation service of process by mail.

The undersigned hereby certifies that the information set forth herein is true and correct and that he or she is authorized to execute this certification on behalf of the Counterparty.

____
Name of Counterparty

By:___________________________
Name:
Title:
Date:

Re: Counterparty briefer example (SocGen) E682FFCF16249F85852576AE007A73B2

Alejandro
LaTorre

Jakobishvili, Nugzari

11/04/2008 02:03 PM

"Doty, Chris", "Paltrowitz, Mark", "Wiedman, Mark", "Jajow, Martin", "Pearl, Morris", "Bloch, Omri", Paul.Whynott, "Villacorta Roland", "Mullin, Stacey", Steven.Manzari, "Buchwald, Zach "

Show Details

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Thanks Nugi: Three reactions/comments: First, can we include a slide between slides 2 and 3 that summarizes key highlights from the data that follows. For example, we'd like a slide that answers to following consistently across counterparties. It is important than in responding to these questions, it provide context, so we're not looking for a simple yes or no For example, in answering question 4 for Soc Gen. we might say it has more AAA than what is in the portfolio for all counterparties, and this implies that it could be more difficult to extract a concession - in other words in the response we want to get to the implication in terms of what we are trying to achieve. 1 Are there large differences between collateral posted and requested and if yes, in what amount?2. Are Blackrock's marks closer to the posted or the requested? 3. Which asset type has the highest concentration relative to the portfolio as a whole (i.e. other counterparties)?4. Is there more or less AAA than in the portfolio as a whole (i.e. other counterparties)? 5. What vintage is the portfolio concentrated in the most and how does this compare to the entire portfolio? 6. Are losses on the CDOs as estimated by blackrock on its scenarios higher or lower than the portfolio as a whole?7. Size of estimated credit events per your base, stress, extreme stress results per year for the next 10 years The issue is that in a meeting, not sure if our management will comb through the data, although we plan on walking them through it. Second, on the discussions to date slide can we standardize across counterparties to address the following points; really just generalizing/reorganizing what you've provided. 1. Your assessment of their negotiating position and rationale - would they accept a concession and why (when you use anecdotal info, be clear consistently like you have down for this slide)? Here you could discuss the status of past negotiations and what the sticking points were. 2. What concession would you think they would accept based on/related to 1. and your understanding of the assets? 3. If they agreed to a deal, whether they had access to assets and whether they have been pledged to third parties (recognizing you may not have complete info). 4. Idiosyncratic/firm specific factors that should impinge on the discussion: e.g.- Synthetic deals, project max and the CRE CDO exposure, existing disputes, etc. Lastly, can we provide the bond level marks and cashflow projections detail to slide 3 in that slide. If there are any questions, or if we are missing something important, let us know. Thanks start upfront with your assessment of the negotiating position Alex LatorreFederal Reserve Bank of New YorkOffice: 212-720-2728Cell: 917-916-0760

"Jakobishvili, Nugzari" <nugzari.jakobishvili@blackrock.com>

11/04/2008 12:57 PM

To

<Paul.Whynott@ny.frb.org>, <Steven.Manzari@ny.frb.org>, <Alejandro.LaTorre@ny.frb.org>

cc

"Wiedman, Mark" <Mark.Wiedman@blackrock.com>, "Buchwald, Zach" <zach.buchwald@blackrock.com>, "Mullin, Sta
"Pearl, Morris" <morris.pearl@blackrock.com>, "Jajow, Martin" <martin.jajow@blackrock.com>, "Palirowitz, Mark" <Mar
<Roland.Villacorta@blackrock.com>, "Bloch, Omri" <omri.bloch@blackrock.com>

Subject

Counterparty briefer example (SocGen)

Steve, Paul, Alex, I've attached a draft of a 3-page counterparty briefer for Societe Generale, with bond-level detail in the appendix. Let us know if this is what you had in mind for the short briefer and we'll produce them for each counterparty. Best, -Nugi
<<Counterparty Briefer - SocGen_110408.ppt>> Nugi Jakobishvili BlackRock 55 East 52nd Street New York, NY 10055 (212) 810-8164 nugzari.jakobishvili@blackrock.com THE INFORMATION CONTAINED IN THIS MESSAGE AND ANY ATTACHMENT MAY BE PRIVILEGED, CONFIDENTIAL, PROPRIETARY OR OTHERWISE PROTECTED FROM DISCLOSURE. If the reader of this message is not the intended recipient, you are hereby notified that any dissemination, distribution, copying or use of this message and any attachment is strictly prohibited. If you have received this message in error, please notify us immediately by replying to the message and permanently delete it from your computer and destroy any printout thereof. - Counterparty Briefer - SocGen_110408.ppt

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Maiden Lane III

Counterparty Briefers

November 5, 2008

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Societe Generale

BLACKROCK SOLUTIONS

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Societe Generale Negotiations

Negotiating Position: Societe Generale (Soc Gen) views the substantial expected recoveries on CDOs and the funding benefit from collateral posting as providing great negotiating leverage

- Soc Gen believes expected recoveries will exceed collateral shortfalls under the CDS. BlackRock cash flow projections support this view
  - Cash flow projections discounted at bond coupon in the base case indicate that Soc Gen's portfolio is of higher quality than other counterparties (based on projected value of 89% for Soc Gen vs. 86% for all counterparties)
- The funding benefit Soc Gen receives from AIG on collateral posted is the spread between LIBOR and Fed funds (Soc Gen receives LIBOR and pays AIG Fed funds)

Concessions: Soc Gen has been unwilling to sell reference CDOs to AIG below par

- Soc Gen would be resistant to deep concessions, i.e., anything greater than a few points, because it believes economic value from collateral and expected recoveries on CDOs are worth more than par in some cases
- Soc Gen expressed willingness to unwind lowest-quality trades at an effective price of ~90 but only if it retains the reference CDOs (i.e., for a CDO priced at 30%, Soc Gen keeps 70% collateral, receives 23% more in cash from AIG, keeps the bond and the upside, and rips up CDS with AIG). This arrangement would not be acceptable under the contemplated structure of Maiden Lane III.

Access to the Assets: We believe that Soc Gen owns most of the reference assets in its portfolio (~$14bn of $16.4bn)

- ~$2bn worth of reference assets may have been sold to Goldman Sachs
- We have heard second-hand from a trader that Soc Gen has pledged much of the portfolio to the Fed discount window for future liquidity

Other Factors

- Soc Gen and AIG are currently in dispute over existing events of default and credit events under trans[illegible] for 2 deals, totaling ~$650M of notional exposure

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Societe Generale Portfolio Overview

Societe Generale is the largest counterparty

- $16.4 billion, representing 25% of total counterparty exposure

$1.4 billion in additional collateral has been requested, but not posted as of 10/24

- Societe Generale has received collateral independent amounts from a number of bonds that have been downgraded
- BlackRock's projected values are in line with values implied by collateral posted, but higher than collateral requested, i.e., BlackRock expects the portfolio to perform better than values implied by requested collateral

In the base case, Societe Generale's portfolio has similar expected losses to the overall portfolio, but in stress cases, Societe Generale's portfolio deteriorates more rapidly than the overall portfolio

Societe Generale's portfolio is heavily concentrated in subprime RMBS and in earlier vintages

- 52% of the portfolio is comprised of residential subprime securities, compared to only 36% for all counterparties
- 28% of the portfolio is concentrated in the 2004 vintage, compared to just 18% for all counterparties

There are fewer high quality assets in Societe Generale's portfolio on a relative basis, but the bottom of the credit spectrum resembles the overall portfolio

- Only 21% of Societe Generale's portfolio is rated AAA (vs. 36% overall)
- But below Investment Grade is identical between Societe Generale and the total portfolio (38%)

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Societe Generale Portfolio vs. All Portfolios

Exposure and Collateral Posting Totals

	Exposure	Rank	Collateral Posted (9/16)	Collateral Posted (10/24)	Collateral Requested (10/24)	Implied CDO Fund Value Based On: Collateral Posted (9/16)	Collateral Posted (10/24)	Collateral Requested (10/24)	BlackRock Analysis
All Counterparties	66,900		17,494	30,254	34,39[illegible]	49,645	16,646	30,301	33,05[illegible]
Societe Generale	16,384	1	4,375	6,375	9,26[illegible]	12,118	4,381	6,632	7,49[illegible]
Percent of Total	24.5%	1	24.5%	27.7%	28.4%	24.5%	21.9%	20.4%	24.2%

Prices implied by Collateral Posting vs. BlackRock Model Price

	Implied Price: 9/16 Collateral Posted	10/24 Collateral Posted	10/24 Collateral Requested	IRR used to discount CFs	BlackRock Model Price: Base CFs Discounted for IRR	Extreme Stress CFs Discounted at Bond Coupon
All Counterparties	74	53	47	11%	67	53
Societe Generale	74	49	46	11%	69	37

BlackRock Cashflow Projections

	Cashflows Discounted at Bond Coupon (% of Current Face): Base	Stress	Extreme Stress	Expected Principal Losses: Base	Stress	Extreme Stress	Collateral Principal Losses: Base	Stress	Extreme Stress
All Counterparties	81	76	53	32	46	54	26	34	44
Societe Generale	84	76	57	35	57	48	25	31	56

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Societe Generale Portfolio vs. All Portfolios

Sector

	Exposure	[illegible]	CMBS	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	Other
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Ratings

	Exposure	Aaa	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	NR
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Societe Generale	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Vintage

	Exposure	2001	2002	2003	2004	2005	2006	2007	2008	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Societe Generale	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

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Goldman Sachs

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Goldman Sachs Negotiations

Negotiating Position: Goldman Sachs is the least risk averse counterparty, i.e., the only counterparty willing to tear up CDS with AIG at agreed-upon prices and retain CDO exposure

- Goldman approached AIG in August to discuss tearing up the CDS contracts
- BlackRock has advised AIG on tearing up 9 CDS in the Goldman portfolio with a $3bn notional
  - These transactions were selected because they were distressed positions likely to experience credit events and convert to cash positions in the next few years (converting to cash positions reduces any basis between the CDO and CDS values)
  - The bid-offer spread between AIG and Goldman on these CDS tear-ups is ~$300 million
- Goldman has expressed a willingness to negotiate tear-ups on additional trades (including 7 synthetic Abacus transactions)

Concessions: Goldman would likely accept a small concession but may look to its funders to absorb the loss (or a portion of the loss)

- Goldman's exposure to AIG is limited to the difference between collateral requested (what they are likely posting to swap counterparties) and collateral received at any given time from AIG. While hedging this AIG counterparty risk is expensive, the cost would translate into no more than 2 points on the whole portfolio
- Goldman's swap counterparties are exposed to Goldman Sachs rather than AIG counterparty risk, and are therefore less likely to be receptive to deep concessions

Access to the Assets: Goldman has said that it does not hold the cash CDOs, but has back-to-back swaps on most of the positions

Other Factors

- Because Goldman prices have been consistently lower than third-party prices, Goldman and AIG have negotiated a collateral posting protocol in which Goldman's prices are given a 12% positive haircut for collateral posting. Goldman's requested collateral amount, therefore, is generally 12% higher than the agreed collateral posting at any given time

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Goldman Sachs Portfolio Overview

Goldman Sachs is the second largest counterparty

- $14.5 billion, representing 72% of total counterparty exposure

$1.3 billion in additional collateral has been requested, but not posted as of 10/24

- Goldman's collateral request does not reflect any haircut to Goldman prices per the protocol established with AIG, so at least a 12% gap attributable to the haircut will remain as long as the haircut protocol is effective
- BlackRock's projected values are higher than collateral requested, i.e., BlackRock expects the portfolio to perform better than values implied by requested collateral

The portfolio is projected to experience higher tranche principal losses than the overall portfolio in all cases (e.g., 15% higher than the total portfolio in the base case)

Despite a significant concentration in prime/agency RMBS, the overall quality of the portfolio is impaired by a large exposure to Alt-A RMBS

- 29% of the Goldman portfolio is prime/agency securities concentrated in a few high-quality CDOs, compared to only 17% for the total portfolio
- However, another 26% of the portfolio is comprised of Alt-A RMBS (vs. 17% of the total)
- Additionally, 55% of Goldman's portfolio is concentrated in 2005 vintage assets (compared to 38% total)

By rating, Goldman's portfolio is barbelled

- 38% of assets rated AAA (compared to 36%), but 25% are below Investment Grade (compared 18%)

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Goldman Sachs Portfolio vs. All Portfolios

Exposure

	Exposure	Rank	Collateral Posted (9/16)	Collateral Posted (10/24)	Collateral Requested (10/24)	Collateral Posted (9/16)	Collateral Posted (10/24)	Collateral Requested (10/24)	BlackRock Intrinsic
						Implied CDO Spread/Value Based On			
All Counterparties	[illegible]		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Goldman Sachs	[illegible]	2	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Percent of Total	[illegible]	2	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Prices

	Implied Price				BlackRock Model Price	
	9/16 Collateral Posted	10/24 Collateral Posted	10/24 Collateral Requested	IRR used to discount CFs	Base CFs Discounted for IRR	Extreme Stress CFs Discounted at Bond Coupon
All Counterparties	54	[illegible]	49	N/A	[illegible]	[illegible]
Goldman Sachs	58	[illegible]	37	N/A	[illegible]	60

Cashflow Projections

	Cashflows Discounted at Bond Coupon (% of Current Face)			Cumulative Principal Losses			Collateral Principal Losses		
	Base	Stress	Extreme Stress	Base	Stress	Extreme Stress	Base	Stress	Extreme Stress
All Counterparties	[illegible]	74	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Goldman Sachs	[illegible]	73	50	[illegible]	59	[illegible]	[illegible]	[illegible]	[illegible]

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Goldman Sachs Portfolio vs. All Portfolios

Sector

	Exposure	Resi - Subprime	CMBS	Resi - Alt-A	Other Resi (Prime/Agency)	Inside CDOs	ABS (Student Loans, Auto, Credit Cards)	Manuf Housing	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Goldman Sachs	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Rating

	Exposure	Aaa	Aa1	Aa2	Aa3	A1	A2	A3	Baa1	Baa2	Baa3	Below Baa3	NR
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Goldman Sachs	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Vintage

	Exposure	2001	2002	2003	2004	2005	2006	2007	2008	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Goldman Sachs	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

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Deutsche Bank

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Deutsche Bank Negotiations

Negotiating Position: Since AIG owns the funded portions of the reference CDOs, terminating Deutsche Bank's financing facility will involve little negotiation

- Deutsche is financing AIG's position in 2a7 deals, including Project Max (which comprises the vast majority of Deutsche's portfolio with AIG)
- AIG believes that there are no early termination penalties for ending the funding facility
- If it were not terminated, Deutsche Bank's financing would roll off 3 to 6 years in a staggered fashion (and AIG would fund the reference CDOs piecemeal over that period)

Concessions: Thus far, Deutsche has not been approached to unwind the facility because of the liquidity benefit that Deutsche has provided to AIG

- Because Deutsche's funding commitment to AIG consumes a large amount of firm capital, we believe Deutsche would be amenable to some concession on the sales
- Deutsche's financing facility has allowed AIG to delay completely funding the Project Max trade and other 2a7 deals (although AIG has posted ~\$2.8bn collateral to Deutsche)
- AIG would be the party to sell the reference CDOs into any structure, after providing to Deutsche the full notional balance (minus any collateral already posted) that Deutsche has funded

Access to the Assets: Based on anecdotal information, we believe that Deutsche is holding the reference CDOs

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Deutsche Bank Portfolio Overview

Deutsche Bank is the third largest counterparty

- $7.6 billion, representing 11% of total counterparty exposure
- Almost all of the exposure is comprised of the Project Max CDO, with is backed by AAA CMBS / CRE

$0.1 billion in additional collateral has been requested, but not posted as of 10/24

- Although Project Max is not expected to experience any principal losses, collateral posting is driven by CMBX spreads
- The difference between BlackRock's model price in the base case and extreme stress case reflect a higher discount rate applied to the base case cashflows associated vs. discounting at LIBOR for the extreme stress case

Deutsche's portfolio has virtually no forecast tranche principal losses in all cases

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Deutsche Bank Portfolio vs. All Portfolios

Exposure

	Exposure	Rank	Collateral Posted (9/18)	Collateral Posted (10/24)	Collateral Requested (10/24)	Implied CDO Bond Value Based On: Collateral Posted (9/14)	Collateral Posted (10/24)	Collateral Requested (10/24)	BlackRock Intrinsic
All Counterparties	65,400		17,154	20,254	34,394	41,445	36,446	33,534	13,079
Deutsche	7,530	3	621	2,023	2,9[illegible]	7,0[illegible]	4,815	4,778	6,310
Percent of Total	[illegible]	3	3.4%	9.8%	[illegible]	16.2%	[illegible]	[illegible]	[illegible]

Prices

	Implied Price: 9/14 Collateral Posted	10/24 Collateral Posted	10/24 Collateral Requested	IRR used to discount CFs	BlackRock Model Price: Base CFs Discounted for IRR	Extreme Stress CFs Discounted at Bond Coupon
All Counterparties	74	55	43	14%	49	63
Deutsche	92	62	62	18%	57	[illegible]

Cashflow Projections

	Cashflow Discounted at Bond Coupon (% of Current Face): Base	Stress	Extreme Stress	Tranche Principal Losses: Base	Stress	Extreme Stress	Collateral Principal Losses: Base	Stress	Extreme Stress
All Counterparties	86	76	65	30	41	34	21	31	46
Deutsche	100	100	97	0	1	3	1	[illegible]	6

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Deutsche Bank Portfolio vs. All Portfolios

Sector

	Exposure	Resi - Subprime	CMBS	Resi - Alt A	Other Resi (Prime/Agency)	Invest. CDOs	ABS (Student Loans, Auto, Credit Cards)	Manuf Housing	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Deutsche	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Rating

	Exposure	Aaa	Aa1	Aa2	Aa3	A1	A2	A3	Baa1	Baa2	Baa3	Below Baa3	NR
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Deutsche	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Vintage

	Exposure	2001	2002	2003	2004	2005	2006	2007	2008	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Deutsche	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Merrill Lynch

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Merrill Lynch Negotiations

Negotiating Position: Merrill Lynch feels that its inexpensive financing and collateral received from AIG limits any incentive to unwind trades at less than par

- Merrill has indicated that in some cases it has locked in inexpensive, long-term financing for the CDOs for which it has purchased protection from AIG. In other cases, Merrill's financing is short-term
- In discussions regarding sale of the reference CDOs, Merrill was not willing to extend financing under any terms to AIG

Concessions: Merrill has been unwilling to sell reference CDOs to AIG below par

- Like Societe Generale, Merrill will likely be resistant to deep concessions because they are satisfied with the current arrangement, but may be receptive to a small concession
- Merrill was not interested in tearing up any CDS with AIG and keeping the reference CDOs

Access to the Assets: Based on discussions with traders, Merrill owns many of the reference CDOs and finances them with third-party banks and conduits

Merrill Lynch Portfolio Overview

Merrill Lynch is the fourth largest counterparty

- $6.4 billion, representing 18% of total counterparty exposure

There have been no additional collateral requests since 10/24

- Merrill requests collateral in line with its own marks (rather than third-party marks) on the positions
- BlackRock's projects the portfolio to perform worse than values implied by collateral requested

Merrill's portfolio is projected to experience higher tranche principal losses than the total portfolio under every scenario

The portfolio is heavily overweight subprime and inner CDOs

- 47% of the portfolio is concentrated in subprime RMBS (compared to 36% overall)
- 20% of the portfolio is comprised of inner CDOs (compared to 10% for the entire portfolio)
- 90% is concentrated in the 2004-2006 vintages (compared to 80% overall)

Only 19% of the portfolio is rated AAA (compared to 36%), while 25% is below Investment Grade (compared to 18% total)

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Merrill Lynch Portfolio vs. All Portfolios

Exposure

	Exposure	Rank	Collateral Posted (9/15)	Collateral Posted (10/24)	Collateral Requested (10/24)	Implied CDO Bond Value Based On: Collateral Posted (9/16)	Collateral Posted (10/24)	Collateral Requested (10/24)	BlackRock [illegible]
All Counterparties	16,900		17,452	20,254	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Merrill Lynch	[illegible]	1	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Percent of Total	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Prices

	Implied Price: 9/10 Collateral Posted	10/24 Collateral Posted	10/24 Collateral Requested	[illegible] used to discount CFs	BlackRock Model Price: Base CFs Discounted for [illegible]	Extreme Stress CFs Discounted at Bond Coupon
All Counterparties	74	53	49	[illegible]	[illegible]	63
Merrill Lynch	69	55	51	[illegible]	[illegible]	[illegible]

Cashflow Projections

	Cashflows Discounted at Bond Coupon (% of Current Face): Base	Stress	Extreme Stress	[illegible] Principal Losses: Base	Stress	Extreme Stress	Collateral Principal Losses: Base	Stress	Extreme Stress
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Merrill Lynch	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Merrill Lynch Portfolio vs. All Portfolios

Sector

	Exposure	Resi-Subprime	CMBS	Resi-Alt A	Other Resi (Prime/Agency)	Inner CDOs	ABS (Student Loans, Auto, Credit Cards)	[illegible]	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Merrill Lynch	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Rating

	Exposure	Aaa	Aa1	Aa2	Aa3	A1	A2	A3	Baa1	Baa2	Baa3	Below Baa3	NR
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Merrill Lynch	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Vintage

	Exposure	2001	2002	2003	2004	2005	2006	2007	2008	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Merrill Lynch	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

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PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

[redacted]

Calyon

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Calyon Negotiations

Negotiating Position: Calyon is highly dependent on AIG collateral posting because of the lower quality of collateral backing its portfolio, and has been aggressive with collateral requests

- Because of independent amounts (IAs) of collateral due to bond downgrades, Calyon's portfolio is well-collateralized by AIG
- Calyon has not been receptive to tearing up the CDS with AIG and retaining the credit risk of its CDO positions

Concessions: Calyon will likely be receptive to a small concession because its portfolio is comprised of CDOs backed by lower quality collateral, but would resist deep concessions because of its overcollateralized position (and because in some cases collateral posting already approaches par)

Access to the Assets: Based on anecdotal information, we believe Calyon owns the reference CDOs

Other Factors:

- For one transaction in the Calyon portfolio (Davis Square V), the bond's downgrade has resulted in AIG's posting of par (bond price = 25 and independent amount upon downgrade = 75, reducing the value to 0)
- AIG has disputed Calyon's collateral request for other transactions in the portfolio (those with marks from Goldman Sachs, since AIG does not give full credit to Goldman's marks for collateral posting purposes). In turn, Calyon will not send the Davis Square V cash CDO to AIG despite the fact that AIG has posted par

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Calyon Portfolio Overview

Calyon is the fifth largest counterparty

- $4.3 billion, representing 7% of total counterparty exposure

$0.3 billion in additional collateral has been requested since 10/24

- Calyon is expected to request more collateral due to independent amounts as bonds have been downgraded
- BlackRock's projected values are significantly higher than Calyon's collateral requests, i.e., BlackRock expects the portfolio to perform better than values implied by collateral requests

Calyon's portfolio is forecast to experience higher tranche principal losses in all scenarios, and exhibits disproportionally worse performance in extreme stress scenarios

The portfolio is heavily overweight subprime and slightly overweight Alt-A

- 56% is subprime (compared to 36% overall)
- 19% is Alt-A, slightly higher than the total portfolio (17%)
- 55% of the portfolio is concentrated in the 2005 vintage (vs. 38% overall)

Only 22% of the portfolio is rated AAA (compared to 36%), and 16% is below Investment Grade (compared to 18% total)

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Calyon Portfolio vs. All Portfolios

Exposure

						Implied CDO Bond Value Based On:			
	Exposure	Rank	Collateral Posted (9/18)	Collateral Posted (10/24)	Collateral Requested (10/24)	Collateral Posted (9/18)	Collateral Posted (10/24)	Collateral Requested (10/24)	BlackRock Intrinsic
All Counterparties	65,307		17,838	30,258	34,398	44,643	36,661	32,556	33,029
Calyon	[illegible]	5	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Percent of Total	[illegible]	5	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Prices

	Implied Price				BlackRock Model Price	
	9/18 Collateral Posted	10/24 Collateral Posted	10/24 Collateral Requested	IRR used to discount CFs	Base CFs Discounted for IRR	Extreme Stress CFs Discounted at Bond Coupon
All Counterparties	54	53	49	165	47	63
Calyon	77	47	40	178	45	[illegible]

Cashflow Projections

	Cashflows Discounted at Bond Coupon (% of Current Face)			Tranche Principal Losses			Collateral Principal Losses		
	Base	Stress	Extreme Stress	Base	Stress	Extreme Stress	Base	Stress	Extreme Stress
All Counterparties	56	76	63	32	46	54	24	34	46
Calyon	50	74	51	37	67	75	26	42	60

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Calyon Portfolio vs. All Portfolios

Sector

	Exposure	[illegible]	CMBS	Alt-A	Other Resi (Prime/Agency)	CDOs	ABS (Student Loans, Auto, Credit Cards)	[illegible]	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Calyon	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Rating

	Exposure	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	Below BBB-	NR
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Calyon	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Vintage

	Exposure	2001	2002	2003	2004	2005	2006	2007	2008	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Calyon	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

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UBS

CONFIDENTIAL PRELIMINARY DRAFT – FOR DISCUSSION PURPOSES

UBS Negotiations

Negotiating Position: UBS has expressed strong interest in providing seller repo-financing to facilitate AIG's purchase of the CDOs in the UBS portfolio

- Although talks are now on hold, the preliminary term sheet contemplated that the difference between par and the collateral posted would be submitted by AIG to UBS in the form of highly rated CLO collateral, held by UBS with a 10% haircut for AAA-rated positions, and a 35% haircut for positions rated AA, A and BBB
- Much of the focus for the repo transaction centers on Triaxx, a CDO that is nearly half of the UBS portfolio ($1.9bn out of $4.2bn), backed by 92% AAA RMBS collateral (57% prime / agency), and is not projected to experience losses in the BlackRock stress case, and little loss in the extreme stress case (value of 95 in the extreme stress case when cash flows are discounted at the bond coupon)

Concessions: Because a significant portion of the UBS portfolio (Triaxx) is very high quality with little expectation of losses, UBS is likely to resist any deep concession

Access to the Assets: Based on negotiations with UBS, we believe that UBS has repo'ed parts of the portfolio (Triaxx and Ischus), but has access to the reference CDOs

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

UBS Portfolio Overview

UBS is the sixth largest counterparty
- $4.2 billion, representing 6% of total counterparty exposure

$0.6 billion in additional collateral has been requested since 10/24
- BlackRock expects the portfolio to perform slightly worse than values implied by collateral requested to date

UBS's portfolio is projected to perform in line with the overall portfolio in each scenario

The portfolio is heavily overweight prime/agency and Alt-A RMBS, with a concentration in 2005 and 2006 vintages
- 30% in each Alt-A and prime/agency (compared to 17% each for the overall portfolio)
- The portfolio is overweight 2006 (35% vs. 23% overall) and underweight 2004 (12% vs. 18% overall)

While 45% of the portfolio is rated AAA (compared to 36%), 21% is below Investment Grade (compared to 18% total)
- AAA assets are found in the Fruix CDO, while the other CDOs in the portfolio are of significantly lower quality

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UBS

Exposure

	Exposure	Rank	Collateral Posted (9/16)	Collateral Posted (10/24)	Collateral Requested (10/24)	Implied CDS Bond Value Based on: Collateral Posted (9/16)	Collateral Posted (10/24)	Collateral Requests & (10/24)	BlackRock Analysis
All Counterparties	[illegible]		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
UBS	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Percent of Total	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Prices

	Implied Price: 9/16 Collateral Posted	10/24 Collateral Posted	10/24 Collateral Requested	BlackRock Model Price: SR used to discount CFs	Base CFs Discounted for IRR	Extreme Stress CFs Discounted at Bond Coupon
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
UBS	[illegible]	[illegible]	[illegible]	[illegible]	47	[illegible]

Cashflow Projections

	Cashflows Discounted at Bond Coupon (% of Current Face): Base	Stress	Extreme Stress	Cumulative Principal Losses: Base	Stress	Extreme Stress	Collateral Principal Losses: Base	Stress	Extreme Stress
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
UBS	88	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	48

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UBS

Sector

	Exposure	[illegible] Subprime	CMBS	Resi Alt-A	Other Resi (Prime/Agency)	[illegible] CDOs	ABS (Student Loans, Auto, Credit Cards)	Muni/ Housing	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
UBS	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Rating

	Exposure	Aaa	Aa1	Aa2	Aa3	A1	A2	A3	Baa1	Baa2	Baa3	Below Baa3	NR
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
UBS	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Vintage

	Exposure	2001	2002	2003	2004	2005	2006	2007	2008	Other
All Counterparties	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
UBS	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

BlackRock Solutions

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Appendices

BLACKROCK SOLUTIONS

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Societe Generale Appendix

BLACKROCK SOLUTIONS

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Societe Generale CSA Overview from Davis Polk

CSA Overview

[illegible]

BLACKROCK SOLUTIONS

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Goldman Sachs Appendix

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Goldman Sachs CSA Overview from Davis Polk

CSA Overview

[illegible]

BLACKROCK SOLUTIONS

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Deutsche Bank Appendix

CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Deutsche Bank CSA Overview from Davis Polk

CSA Overview

BLACKROCK SOLUTIONS

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Merrill Lynch Appendix

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CONFIDENTIAL

PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

Merrill Lynch CSA Overview from Davis Polk

CSA Overview

[illegible]

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Calyon Appendix

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Calyon CSA Overview from Davis Polk

CSA Overview

[illegible]

UBS Appendix

BLACKROCK SOLUTIONS

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CONFIDENTIAL PRELIMINARY DRAFT - FOR DISCUSSION PURPOSES

UBS CSA Overview from Davis Polk

CSA Overview

BLACKROCK SOLUTIONS

555

James P Bergin/NY/FRS
11/05/2008 08:58 PM

To: Thomas Baxter/NY/FRS@FRS
cc: Joyce Hansen/NY/FRS@FRS, HaeRan Kim/NY/FRS@FRS, Jennifer Wolgemuth/NY/FRS@FRS
bcc:
Subject: Fw: ML III - draft confidentiality agreement

Tom,

I understand that you and Terry may be having conversations with AIG-FP counterparties tomorrow. In case you are, attached is a draft confidentiality agreement that could be used. We drafted it, and DPW reviewed it and made a few helpful suggestions. One question I have, however, is whether the confidentiality agreement should be addressed to AIG as well. Depending on your answer to this, I can make a few conforming changes tomorrow.

Also, my understanding is that FRBNY will have bilateral discussions with the counterparties w/o AIG. I asked Marshall Huebner whether he felt we should get some direction from AIG that we could have these conversations (I understand that you mentioned this idea to HaeRan). He felt that it was a good idea to get an email but he felt that we didn't need anything more than that. His analysis was basically that we are already very pregnant, so lender liability concerns can't be at the front of our concerns, but that some paper trail would be nice to have.

Thanks,
Jim
----- Forwarded by James P Bergin/NY/FRS on 11/05/2008 08:47 PM -----

"Chenard, James" <james.chenard@dpw.com>
11/05/2008 05:52 PM

To: <James.Bergin@ny.frb.org>
cc: <Paul.Whynott@ny.frb.org>, <alejandro.latorre@ny.frb.org>, <Danielle.Vicente@ny.frb.org>, <haeran.kim@ny.frb.com>, <joyce.hansen@ny.frb.com>, "Bjerke, Bjorn" <bjorn.bjerke@dpw.com>, "Anderson, Paul" <paul.anderson@dpw.com>
Subject: Re: ML III - draft confidentiality agreement

Attached please find a clean and blackline of the draft confidentiality agreement, reflecting a few comments we had. Please let us know if you have any questions. Thanks.

Best regards,
Jim

James Chenard
Davis Polk & Wardwell
450 Lexington Avenue
New York, New York 10017
p. 212.450.4596 | f. 212.450.3596 MLIII Confidentiality Agreement.blk.DOC MLIII.Confidentiality.Agreement.DOC

James P Bergin/NY/FRS

11/05/2008 09:05 PM

To: HaeRan Kim/NY/FRS@FRS

cc: Jennifer Wolgemuth/NY/FRS@FRS, Joyce Hansen/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS

bcc

Subject: Re: Fw: ML III - draft confidentiality agreement000000000003FFFF006E00137CE00000

Yes, sorry, I should have mentioned that as well.

HaeRan Kim/NY/FRS

11/05/2008 09:04 PM

To: James P Bergin/NY/FRS@FRS

cc: Jennifer Wolgemuth/NY/FRS@FRS, Joyce Hansen/NY/FRS@FRS, Thomas Baxter/NY/FRS@FRS

Subject: Re: Fw: ML III - draft confidentiality agreement

At today's conference call with Board staff, they mentioned that Scott had some reservations about FRBNY reps having negotiation discussions with supervised institutions. I understood that Scott was trying to follow up on this with Tom.

James P Bergin/NY/FRS

11/05/2008 08:59 PM

To: Thomas Baxter/NY/FRS@FRS

cc: Joyce Hansen/NY/FRS@FRS, HaeRan Kim/NY/FRS@FRS, Jennifer Wolgemuth/NY/FRS@FRS

Subject: Fw: ML III - draft confidentiality agreement

Tom,

I understand that you and Terry may be having conversations with AIG-FP counterparties tomorrow. In case you are, attached is a draft confidentiality agreement that could be used. We drafted it, and DPW reviewed it and made a few helpful suggestions. One question I have, however, is whether the confidentiality agreement should be addressed to AIG as well. Depending on your answer to this, I can make a few conforming changes tomorrow.

Also, my understanding is that FRBNY will have bilateral discussions with the counterparties w/o AIG. I asked Marshall Huebner whether he felt we should get some direction from AIG that we could have these conversations (I understand that you mentioned this idea to HaeRan). He felt that it was a good idea to get an email but he felt that we didn't need anything more than that. His analysis was basically that we are already very pregnant, so lender liability concerns can't be at the front of our concerns, but that some paper trail would be nice to have.

Thanks,
Jim
----- Forwarded by James P Bergin/NY/FRS on 11/05/2008 08:47 PM -----

"Chenard, James" <james.chenard@dpw.com>

11/05/2008 05:52 PM

To

<James.Bergin@ny.frb.org>

cc

<Paul.Whynott@ny.frb.org>, <alejandro.latorre@ny.frb.org>, <Danielle.Vicente@ny.frb.org>, <haeran.kim@ny.frb.com>, <joyce.hansen@ny.frb.com>, "Bjerke, Bjorn" <bjorn.bjerke@dpw.com>, "Anderson, Paul" <paul.anderson@dpw.com>

Subject

Re: ML III - draft confidentiality agreement

Attached please find a clean and blackline of the draft confidentiality agreement, reflecting a few comments we had. Please let us know if you have any questions. Thanks.

Best regards,
Jim

James Chenard
Davis Polk & Wardwell
450 Lexington Avenue
New York, New York 10017
p. 212.450.4596 · f. 212.450.3596[attachment "MLIII.Confidentiality.Agreement.blk.DOC" deleted by James P Bergin/NY/FRS] [attachment "MLIII.Confidentiality.Agreement.DOC" deleted by James P Bergin/NY/FRS]

Ethan, What do we have to do to paper the AIG authority to let us negotiate on their behalf for ML3? - Steve

Steven J Manzari

t
o
:

ethan.james

11/06/2008 09:16 AM

Show Details

Steven J. Manzari
Federal Reserve Bank of New York
33 Liberty Street
New York, NY 10045
T 212 720 5881
F 212 720 7922
C 646 701 4635
24 HR FRBNY CENTRAL WATCH 212 720 2222

Fw: ML III over the next few days

Paul Whynott

Steven J Manzari

11/06/2008 02:46 PM

Show Details

560

FYI

Paul Whynott
Federal Reserve Bank of New York
Work (212) 720-2388
Cell (914) 715-9886
Berry (917) 254-6896

----- Forwarded by Paul Whynott/NY/FRS on 11/06/2008 02:42 PM -----

Paul Whynott/NY/FRS

11/06/2008 02:46 PM

To

"Wiedman, Mark" <Mark.Wiedman@blackrock.com>, Skip.Curth@ey.com, "Bjerke, Bjorn" <bjorn.bjerke@dpw.com>

cc

"Paltrowitz, Mark" <Mark.Paltrowitz@blackrock.com>, "Villacorta, Roland" <Roland.Villacorta@blackrock.com>, "Buchwald, Zach " <zach.buchwald@blackrock.com>, "Jajow, Martin" <martin.jajow@blackrock.com>, "Jakobishvili, Nugzari" <nugzari.jakobishvili@blackrock.com>, joe.palumbo@ey.com, richard.gonseth@ey.com, Brian.Paul@ey.com, Alejandro LaTorre/NY/FRS@NY, Paul Whynott/NY/FRS@NY, Danielle Vicente/NY/FRS@FRS, Michael Alix/NY/FRS@FRS, Julie Dolan/NY/FRS@NY, James P Bergin/NY/FRS@FRS, Jennifer Wolgemuth/NY/FRS@NY, Clinton Lively/NY/FRS@FRS, Maria Ambrosio/NY/FRS@NY

Subject

ML III over the next few days

All,

as we proceed with Maiden Lane III, and reach out to counterparties, we will need considerable support from now through at least Monday morning. It is unclear at this point what the level of questions and interaction will be with the counterparties and whether we will need representatives on-site at the FRBNY through the weekend or on call. My sense is that there will be an active dialogue to ensure we agree on the portfolio of transactions and the collateral posted against those specific transactions. Once offers are in we will need to quickly analyze and make recommendations for management approval.

BlackRock: Zach and Nugi, we will reserve a conference room here at the Fed for you to use as needed. Given the potential downtime - I assume it is most efficient for you to work remotely from your offices and come down as necessary. Open to suggestions if you see a better approach.

E&Y: Already have space onsite. We anticipate that there will likely be a substantial amount of reconciliation of trades early in the process.

DPW: Bjorn - feel free to set up in our conference room as needed on 13. We can arrange for a conference room if you require additional space here

561

Thank you all in advance,

Paul

Paul Whynott
Federal Reserve Bank of New York
Work (212) 720-2388
Cell (914) 715-9886
Berry (917) 254-6896

"Wiedman, Mark"
<Mark.Wiedman@blackrock.com>

11/06/2008 04:35 PM

To
<Paul.Whynott@ny.frb.org>, <Skip.Curth@ey.com>, <bjorn.bjerke@dpw.com>

cc
"Paltrowitz, Mark" <Mark.Paltrowitz@blackrock.com>, "Villacorta, Roland" <Roland.Villacorta@blackrock.com>, "Buchwald, Zach " <zach.buchwald@blackrock.com>, "Jajow, Martin" <martin.jajow@blackrock.com>, "Jakobishvili, Nugzari" <nugzari.jakobishvili@blackrock.com>, <Joe.Palumbo@ey.com>, <richard.gonseth@ey.com>, <Brian.Paul@ey.com>, <Alejandro.LaTorre@ny.frb.org>, <Danielle.Vicente@ny.frb.org>, <Michael.Alix@ny.frb.org>, <Julie.Dolan@ny.frb.org>, <James.Bergin@ny.frb.org>, <Jennifer.Wolgemuth@ny.frb.org>, <Clinton.Lively@ny.frb.org>, <Maria.Ambrosio@ny.frb.org>

bcc

Subject
Re. ML III over the next few days

Paul - as we discussed, please just copy our whole squad over the weekend so we are sure to serve you best.Roland VZach BNugi JMark PMark W (me)Morris PearlStacey MullinMarty Jajow

From: Paul.Whynott@ny.frb.org **To**: Wiedman, Mark; Skip.Curth@ey.com ; Bjerke, Bjorn **Cc**: Paltrowitz, Mark; Villacorta, Roland; Buchwald, Zach ; Jajow, Martin; Jakobishvili, Nugzari; joe.palumbo@ey.com ; richard.gonseth@ey.com ; Brian.Paul@ey.com ; Alejandro.LaTorre@ny.frb.org ; Paul.Whynott@ny.frb.org ; Danielle.Vicente@ny.frb.org ; Michael.Alix@ny.frb.org ; Julie.Dolan@ny.frb.org ; James.Bergin@ny.frb.org ; Jennifer.Wolgemuth@ny.frb.org ; Clinton.Lively@ny.frb.org ; Maria.Ambrosio@ny.frb.org **Sent**: Thu Nov 06 14:46:02 2008**Subject**: ML III over the next few day! s All,as we proceed with Maiden Lane III, and reach out to counterparties, we will need considerable support from now through at least Monday morning. It is unclear at this point what the level of questions and interaction will be with the counterparties and whether we will need representatives on-site at the FRBNY through the weekend or on call. My sense is that there will be an active dialogue to ensure we agree on the portfolio of transactions and the collateral posted against those specific transactions. Once offers are in we will need to quickly analyze and make recommendations for management approval. BlackRock: Zach and Nugi, we will reserve a conference room here at the Fed for you to use as needed. Given the potential downtime - I assume it is most efficient for you to work remotely from your offices and come down as necessary. Open to suggestions if you see a better approach. E&Y: Already have space onsite. We anticipate that there will likely be a substantial amount of reconciliation of trades early in the process. DPW: Bjorn - feel free to set up in our conference room as needed on 13. We can arrange for a conference room if you require additional space here. Thank you all in advance. PaulPaul WhynottFederal Reserve Bank of New YorkWork (212) 720-2388Cell (914) 715-9886Berry (917) 254-6896THE INFORMATION CONTAINED IN THIS MESSAGE AND ANY ATTACHMENT MAY BE PRIVILEGED, CONFIDENTIAL, PROPRIETARY OR OTHERWISE PROTECTED FROM DISCLOSURE. If the reader of this message is not the intended recipient, you are hereby notified that any dissemination, distribution, copying or use of this message and any attachment is strictly prohibited. If you have received this message in error, please notify us immediately by replying to the message and permanently delete it from your computer and destroy any printout thereof.

James P Bergin/NY/FRS

11/06/2008 09:15 PM

To: Joyce Hansen/NY/FRS@FRS, HaeRan Kim/NY/FRS@FRS, Jennifer Wolgemuth/NY/FRS@FRS

cc

bcc

Subject: Fw: ML III - documents

----- Forwarded by James P Bergin/NY/FRS on 11/06/2008 09:11 PM -----

"Bjerke, Bjorn" <bjorn.bjerke@dpw.com>

11/06/2008 07:10 PM

To: "Buchwald, Zach " <zach.buchwald@blackrock.com>

cc: "Jakobishvili, Nugzari" <nugzari.jakobishvili@blackrock.com>, <joe.palumbo@ey.com>, <Skip.Curth@ey.com>, "Wiedman, Mark" <Mark.Wiedman@blackrock.com>, "Anderson, Paul" <paul.anderson@dpw.com>, <Paul.Whynott@ny.frb.org>, <Alejandro.LaTorre@ny.frb.org>, <Danielle.Vicente@ny.frb.org>, <James.Bergin@ny.frb.org>, "Heckart, Robert L." <robert heckart@dpw.com>

Subject: RE: ML III - documents

Thank you Zach,

Very helpful.

The Termination Payment is actually not defined in the purchase agreement, it is the term used in the Termination Agreement (it was intended as a placeholder for us when we fill in an amount just to remind us that we end up with Initial Purchase Price + CDS termination payment (i.e. Termination Payment) - Concession = par of CDS. Anyway, I will make that clear because good point that this term is not otherwise found in the Purchase Agreement.

As for bonds where there had been a credit event, I viewed those as being settled outside MLIII (by AIG paying par) and remaining outside ML III. Now you raise a good point, would we want ML III to purchase that bond from AIG FP after settlement at a price equal to its market price (i.e. so that AIG, just like in a tear-up, paid the current mark to market loss and ML III buys CDO at market - concession). I don't know the answer so I pose that question to Paul and Alex.

As for the transactions you list, it seems to me that if the C/P are willing to sell at the agreed price, then that issue might resolve itself but if the counterparties use that as an additional argument that they are entitled to par, then indeed that is worth paying attention too. Thanks. Maybe you can give a quick 10 minute run down on the 7:30 call or next update call on how that posturing has played out? Have they delivered credit event notices and demanded physical settlement? Only argued the point?

Best,
Bjorn

From: Buchwald, Zach [mailto:zach.buchwald@blackrock.com]
Sent: Thursday, November 06, 2008 6:28 PM
To: Bjerke, Bjorn
Cc: Jakobishvili, Nugzari; joe.palumbo@ey.com; Skip.Curth@ey.com; Wiedman, Mark
Subject: RE: ML III - documents

Bjorn:

Couple of questions:

What is the "Termination Payment" that is deducted from the Initial Purchase Price? It's not a defined term, and I can't figure out what it refers to.

Under Excluded Assets, you exclude those positions that have experienced credit events. Are those bonds ultimately going to be included in ML3? I don't see any provision under which that would take place. Also – you might want to say explicitly under clause (a) of the definition of Excluded Asset that cash positions that have experienced Events of Default do not qualify as Excluded Assets based solely on the EoD. Also FYI – the counterparties have been arguing with AIG that a handful of transactions that already hit EoD are automatically experiencing credit events under the swaps. This is a gray area under the original transaction documents, and it makes sense for FRB to formulate its position in advance. FYI – these positions are:

TABS 05-4 (Soc Gen)
Independence 5 (GS, Merrill already put to AIG)
MKP CBO (Soc Gen)
Independence 6 (Coral, Merrill)
Neptune 2 (Merrill)
Mercury 2 (BofA)
Straits Global (Merrill)

Otherwise, the pricing provisions look good to me.

Thanks,

Zach Buchwald

Managing Director

BlackRock Solutions

55 East 52nd Street

New York, NY 10055

Tel: 212 810 5650

Email: zach.buchwald@blackrock.com

From: Bjerke, Bjorn [mailto:bjorn.bjerke@dpw.com]
Sent: Thursday, November 06, 2008 4:58 PM
To: Buchwald, Zach
Cc: Jakobishvili, Nugzari; joe.palumbo@ey.com; Skip.Curth@ey.com; Wiedman, Mark
Subject: FW: ML III - documents

FYI

Zach (and all). These first drafts were all completed in a bit of a rush but would you mind in particular focusing on the purchase price/termination price provisions to make sure you agree with the math? There are some minor legal technical comments I have received from the fed in terms of indemnity and jurisdiction clause etc. that I am dealing with, but the most important part of the whole document is the purchase price calculation so any comments you have on that determination is particularly helpful and I am naturally grateful for all additional input.

Best,
Bjorn

From: James.Bergin@ny.frb.org [mailto:James.Bergin@ny.frb.org]
Sent: Thursday, November 06, 2008 4:52 PM
To: Elias.Habayeb@aig.com; jason.smith@weil.com
Cc: Paul.Whynott@ny.frb.org; Steven.Manzari@ny.frb.org; Alejandro.LaTorre@ny.frb.org; Jennifer.Wolgemuth@ny.frb.org; HaeRan.Kim@ny.frb.org; Joyce.Hansen@ny.frb.org; Danielle.Vicente@ny.frb.org; Anderson, Paul; Bjerke, Bjorn
Subject: ML III - documents

Per Steve Manzari's request, attached please find a draft term sheet for the counterparty transactions, forward purchase agreement, and termination agreement for ML III, as drafted by Davis Polk. I believe you received the full term sheet for ML III earlier.

Please note that these are preliminary drafts, and remain subject to review and comment by FRBNY in all respects.

Thanks,
Jim

James P. Bergin
Counsel & Assistant Vice President
Federal Reserve Bank of New York
(212) 720-5017
(212) 720-1756 (fax)

Danielle Vicente/NY/FRS

11/07/2008 11:00 AM

To: Alejandro LaTorre/NY/FRS@FRS, Paul Whynott/NY/FRS@FRS

cc

bcc

Subject: Call elias

I sent this under a different subject line before- see below
Danielle Vicente
Federal Reserve Bank of New York
Office: 212-720-2566
Cell: 347-266-4870

----- Original Message -----
From: Danielle Vicente
Sent: 11/07/2008 10:53 AM EST
To: Paul Whynott; Alejandro LaTorre
Subject: Skip called-traders and DB

The traders are telling the counterparties that they cannot negotiate collateral because their lawyers told them not to.

When you call Elias about DB can you ask for the script their traders are using and see if you are comfortable with it? Thanks
Danielle Vicente
Federal Reserve Bank of New York
Office: 212-720-2566
Cell: 347-266-4870

Alejandro LaTorre/NY/FRS
12/07/2008 05:42 PM

To Richard Charlton/NY/FRS@FRS
cc Danielle Vicente/NY/FRS@FRS
bcc
Subject Re: question about AIG0C0000000003FFFF006E00137CE00000

yes - by paying par this means they kept whatever collateral posted and ML 3 purchased the CDOs at their marks

Alex Latorre
Federal Reserve Bank of New York
Office: 212-720-2728
Cell: 917-916-0760

Sent from my BlackBerry Handheld

----- Original Message -----
From: Richard Charlton
Sent: 12/07/2008 05:28 PM EST
To: Alejandro LaTorre
Cc: Danielle Vicente
Subject: Re: question about AIG

Alex, that's because the counterparties got par? Thanks.

Regards,

Richard Charlton
Counsel and Assistant Vice President
Federal Reserve Bank of New York
(212) 720-2867
(646) 720-2867
(917) 539-8697 (m)
richard.charlton@ny.frb.org

Any views expressed are those of the author and do not necessarily reflect the position of the Federal Reserve Bank of New York or the Federal Reserve System.

Alejandro LaTorre/NY/FRS
12/07/2008 05:04 PM

To Danielle Vicente/NY/FRS@FRS, Richard Charlton/NY/FRS@FRS
cc
Subject Re: question about AIG

That's right. Only clarification I would add is that the 10/31 price has no bearing on the counterparties and what they received but only relevant for AIG and ML 3 in terms of P/L impact and cash collateral returned to AIG

Alex Latorre
Federal Reserve Bank of New York
Office: 212-720-2728
Cell: 917-916-0760

Sent from my BlackBerry Handheld

----- Original Message -----

From: Danielle Vicente
Sent: 12/07/2008 04:26 PM EST
To: Richard Charlton
Cc: Alejandro LaTorre
Subject: Re: question about AIG

Sorry for the delay!

We are using BLACKROCK's 10/31 prices; that's the price at which ML III purchased the underlying CDO bonds. They modeled the underlying cashflows for these CDOs given economic conditions, etc.

AIG did value the portfolio as of 10/31, and although we didn't use their prices, the means used to obtain these AIG prices were verified by E&Y. E&Y helped us "tie out" with the counterparties, making sure everyone was on the same pages with respect to the notional amount of the securities, the collateral posted, and the purchase price.

Does that make sense? Alex do you have a different understanding?

Dani

Danielle Vicente
Phone: 212-720-2566
Mobile: 347-266-4870

Richard Charlton/NY/FRS

12/06/2008 10:08 PM

To Danielle Vicente/NY/FRS@FRS
cc
Subject question about AIG

Dani, who verified the prices of the CDOs--E&Y? Or BlackRock? And can you clarify their respective roles? I need this before Monday morning for a meeting on the Hill. Thanks.

Regards,

Richard Charlton
Counsel and Assistant Vice President
Federal Reserve Bank of New York
(212) 720-2867
(646) 720-2867
(917) 539-8697 (m)
richard.charlton@ny.frb.org

Any views expressed are those of the author and do not necessarily reflect the position of the Federal Reserve Bank of New York or the Federal Reserve System.

James P Bergin/NY/FRS

11/07/2008 07:11 PM

To Jennifer Wolgemuth/NY/FRS@FRS, HaeRan Kim/NY/FRS@FRS, Joyce Hansen/NY/FRS@FRS

cc

bcc

Subject ML III - the latest

I talked briefly to the gentlemen upstairs. The concession negotiations did not go favorably, although the notion of tear-ups was greeted warmly. We've given up on concessions. We will apparently be calling in the counterparties to meetings on Sunday seriatim and asking them to agree to a tear-up at par. Alex and Paul got called into a meeting with Goldman, so I haven't been able to figure out yet what the plan is in terms of documents. I would figure that we'll sign a term sheet, although if we have the documents ready (and we should) we could think about attaching those to the term sheets and saying that the agreement will be in substantially the form thereof. Bjorn told me on the phone that Paul asked him to come down tonight for some reason.

Alejandro LaTorre/NY/FRS
12/15/2008 07:21 PM

To
James P Bergin/NY/FRS@FRS
cc
Danielle Vicente/NY/FRS@FRS, Jennifer Wolgemuth/NY/FRS@FRS
bcc

Subject
Re: what do you think of this....000000000003FFFF006E00137CE00000

Thanks Jim; can we highlight that this is tearing up CDS for CDO like before - this is implicit, but would like to make explicit.

also can/should we say that the only idiosyncratic feature of the note that it is not exactly a CDO, which is something being considered already as part of the proposal being discussed with the Board tomorrow?

Can we also say that there is a sincere desire to close out on the 18th?

Thanks

Alex Latorre
Federal Reserve Bank of New York
Office: 212-720-2728
Cell: 917-916-0760

569

James P Bergin/NY/FRS

12/15/2008 06:44 PM

To Alejandro LaTorre/NY/FRS@FRS, Danielle Vicente/NY/FRS@FRS, Jennifer Wolgemuth/NY/FRS@FRS

cc

Subject what do you think of this....

Rich, Kieran, April,

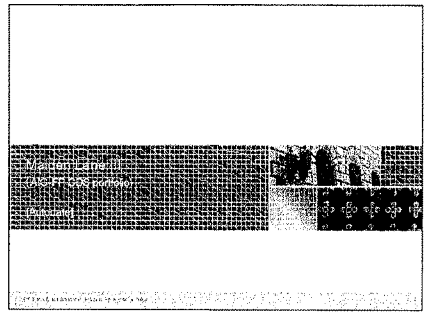
As I spoke about very briefly with April this afternoon, there is an additional feature of one of the "Round 1 fails" of which I wanted to make you aware. Goldman's Hout Bay CDO is a multisector CDO on which AIGFP wrote CDS protection. It was in the list presented to the Board for approval in November, and was scheduled on our Forward Purchase Agreement with Goldman. However, in this case, AIGFP wrote protection on the CDO only to the extent that their par value (which is approximately $1.197 billion) experienced a decline in market value of more than $450 million. Because AIGFP's protection of the notes is limited, it wouldn't make economic sense for ML III to simply buy the CDO at par in exchange for termination of the protection, as in the other deals.

Instead, Goldman is proposing to place the CDO in a trust vehicle that would replicate the economics of the protection they had from AIG, and to sell those notes to Maiden Lane III. That is, Maiden Lane III would receive senior notes of approximately $747 million from the trust vehicle, and Goldman would receive subordinated notes of $450 million. Principal and interest received from the Hout Bay CDOs would run first to the senior holder (ML III) and then to the subordinated holder (Goldman). As a result, ML III would have an indirect interest in the CDO, and AIGFP's protection would terminate. We and our counsel would need to get comfortable that the trust structure accurately captures the economics and risks.

I apologize for not having brought this feature to your attention earlier -- I was distracted working to close Maiden Lane II last week. April tells me that Rich (quite understandably) expressed a desire to defer consideration of this note until you get the rest of Round 2 determined. We don't want to do anything that would hold up the memo that you are preparing for the Governors on the rest of round 1, but the policy folks have also expressed a sincere desire to close out this position this year, if possible.

Thanks,

570



571

1

AIG – CDS Portfolio

- Problem: Liquidity drain from mark to market collateral requirements on CDS
- Objective: Eliminate liquidity drain while mitigating capital impact on AIG
- Considerations:
  - Lend against value
  - First priority in any structured solution is to ensure that Fed funding is repaid in all scenarios
  - No long-term interaction between Fed and counterparties to minimize possible conflicts of interest
  - Counterparties should be nearly indifferent on the solution (i.e. not much relative benefit), but willing to participate
    - Negotiation with counterparties should be minimized if possible
  - ~90% of the CDS are physical settle – thus, counterparties will be exposed to risk if CDS are simply torn-up

2

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AIG – CDS Portfolio

BlackRock has isolated 4 potential structured solutions to explore further:

1. Mezzazine SPV Structure: SPV purchases CDOs at current marks and counterparties take a Mezzanine tranche (AIG takes equity tranche). CDS transactions are torn-up/

2. Two-tier SVP Structure at current marks, similar to the option above but without a Mezzanine tranche: AIG takes a larger equity tranche

3. Mezzezine SPV Structure at a lower transfer price

4. Two-tier SVP Structure at a lower transfer price

- Within each of these structures, we will explore different assumptions for the main levers: tranche sizes, coupons on tranches, etc.

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AIG – CDS Portfolio

- Next steps:
  - Analyze cash flows/returns/risks of the 4 potential structures, under various assumptions for the main levers
  - Understand and gain comfort with BR's modeling approach, with focus on stress vs. extreme stress scenarios and additional data on default, loss results, etc
  - Document execution risks, e.g.
    - Negotiation with counterparties could be very time-consuming
    - Model risk: projections rely heavily on BlackRock models

4

574

Execution Strategy Issues

- Counterparties have different economics:
  - If own underlying reference bond or not
  - If a back-to-back swap with another counterparty
  - Negotiated collateral positions
- Execution strategy, considerations:
  - Need to get a critical mass
  - Consistent approach or outcome
    - Fairness v. playing to the lowest common denominator
  - Sequencing of events

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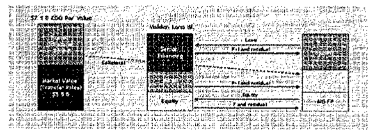
BlackRock – Mezzazine Structure



CDS torn-up

CDO purchased from counterparty into SVP

Special Purpose Vehicle:

- FRBNY provides senior note
- Counterparty provides mezzazine financing
- AIG provides equity tranche

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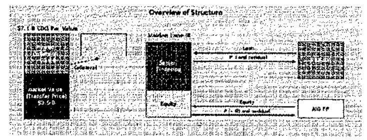
BlackRock – Two-tier Structure



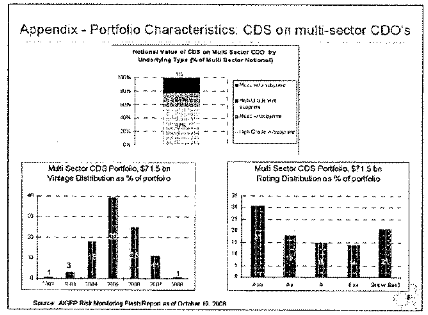
CDS torn-up

CDO purchased from counterparty into SVP

Special Purpose Vehicle:

- FRBNY provides senior note
- AIG provides equity tranche

577


Appendix - Portfolio Characteristics: CDS on multi-sector CDO's
Notional Value of CDS on Multi Sector CDO by Underlying Type (% of Multi Sector Notional)
100%
80%
60%
40%
20%
0%
Multi Sector CDS Portfolio, $71.5 bn
Vintage Distribution as % of portfolio
40
30
20
10
0
1
3
1
2004
2005
Multi Sector CDS Portfolio, $71.5 bn
Rating Distribution as % of portfolio
35
30
25
20
15
10
5
0
Aaa
Aa
A
Source: AIGFP Risk Monitoring Flash Report as of October 10, 2008

Appendix - Top Counterparties to CDS on Multi-Sector CDO's

Counterparty	Notional	Client Mark	AIG Mark	Diff
Goldman Sachs	19,592	10,475	9,297	(1,35[illegible])
Societe Generale	18,568	4,387	8,3[illegible]	(1,3[illegible])
Merrill Lynch International	7,120	3,529	3,529	-
Deutsche	5,305	3,015	2,655	(360)
Calyon	4,330	2,004	2,292	(31[illegible])
UBS	4,218	2,065	1,457	(608)
Barclays	2,455	1,29[illegible]	1,29[illegible]	-
[illegible]	1,805	735	735	-
Bank of Montreal	1,089	504	504	(6)
Rabobank	1,074	349	636	([illegible])
Royal Bank of Scotland	1,038	615	624	(19[illegible])
Wachovia	927	102	10[illegible]	-
Bank of America	776	267	267	-
CIBC	520	433	392	(40)
HSBC Bank	505	311	262	(5[illegible])
Other [illegible]	3,2[illegible]	445	41[illegible]	([illegible])
Total	**71,014**	**37,407**	**33,118**	**(4,287)**

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Notes from follow-up call with Mark W. on ML III

Paul Whynott

to:

Steven J Manzari, Jim Mahoney, Danielle Vicente, Paul Whynott, Skip.Curth, richard.gonseth, Clinton Lively, Alejandro LaTorre, Maria Ambrosio

10/21/2008 02:06 PM

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Tuesday, October 21, 2008
11:15am

Steve, Clint and I had a follow-up call with Mark Wiedman, BlackRock, to follow-up on the 9am discussion.

We expressed our discomfort with the information and options presented thus far and highlighted the need for additional work and a lot more transparency behind their assumptions as well as options they have ruled out and why. We indicated that they should not communicate to the firm these scenarios at this point given our comfort level and the fact that it may be misleading to the firm at this point.

Mark expressed that he understood and appreciated our request. He noted that they were under a lot of time pressure and see the need to provide additional information and transparency. He asked that we reach out to AIG to let them know that we have requested this additional work/information and advised BlackRock not to provide the scenarios to date at this point. Mark noted that concern of appearing unresponsive to AIG as they had committed to and end of day Monday deliverable.

Mark will develop an outline of our request and circulate it to us later today to ensure that we are all on the same page and that they are focused correctly.

Our request did include:

- Getting a better understanding of the fair market value of the CDOs (asking BR to line up AIG's marks, the counterparty marks, and the agreed upon markets)
- Provide more levers on the capital structure – there is a lot of model risk and we want a lot more safety for the FRBNY
- Clarify consolidation issues – lay out more scenarios and indicate why certain options were deemed not worth pursuing.
- Explore doing the trades at off market rates – there is a wide bid-offer spread, explore the range of fair value and a market clearing rate. What would the structure look like if it reflects what new money is willing to invest in these products at?
- Transparency with respect to inputs – HPA assumptions, discount assumptions, etc
- Broader set of options – the current set is very narrow with only minor tweaks between them. Again, explain why the other scenarios are non-starters.
- Asked, again, for an independent evaluation of their base scenario inputs – give some comparison to external benchmarks. They will present assumptions compared to the ABX.
- Do a break the bond/structure scenario – what would it take for the Fed to lose money?

Sorry for the quick brain dump, but I wanted to give folks a quick sense of where we are at.

Paul

Paul Whynott
Federal Reserve Bank of New York
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Cell (914) 715-9886
Berry (917) 254-6896

AIG

DRAFT

To: Files

Cc:

From:

Date: October 22, 2008

Re: AIG Financial Products: Impact of Further Rating Downgrades

Introduction

The purpose of this memorandum is to describe the potential liquidity impact on AIG Financial Products Corp. ("AIGFP") of further rating downgrades of American International Group, Inc. ("AIG"), as well as the efforts underway to confirm the completeness and reasonableness of our analysis.

Following recent events, the current ratings for AIG's long term unsecured debt are the following:

S&P:	A-
Moody's:	A3
Fitch:	A

AM Best rates AIG at bbb, but this rating agency's specialty is insurance companies, and its ratings are not referenced in financial product contracts. A downgrade by Fitch is not expected to have a significant liquidity effect; however, that is being validated by AIGFP's internal and external counsel.

1. Due Diligence Process

AIGFP's internal and external counsel are currently in the process of reviewing documentation related to significant transactions to which AIGFP is a party in order to confirm the completeness of the credit rating triggers reflected in the AIGFP systems used to evaluate liquidity demands in different downgrade scenarios. The status of these efforts is as follows:

- A review of rating triggers has been performed by Weil Gotshal on the entire Super Senior book.

- A review of ISDA Master Agreements and related Credit Support Annexes ("CSAs") has been performed by Weil Gotshal with the goal of covering 90% of the absolute value of the mark to market exposure of derivative trades and checking that documentation is consistent with ratings trigger information that already exists in AIGFP's systems. AIG FP is currently analyzing the noted discrepencies.

- All other significant categories of products are being reviewed either by external or internal lawyers to assess the existence of collateral or termination downgrade triggers. This review covers:

    - o Municipal GICs
    - o Structured lease GICs
    - o Benefit Responsive Option transactions (sometimes references as "BROs" or "Stable Value Wraps")
    - o Issued securities
    - o Repurchase and reverse repurchase transactions
    - o Securities lending transactions
    - o Gold leases
    - o TDG trades, infrastructure investment and other structures trades.

For these categories of transactions, AIGFP, in consultation with AIG corporate personnel, outside counsel and PwC, is determining an approach for documentation review, which is set out in the draft "Scope of Review" document in appendix to this memorandum. The draft document remains subject to further review.

2. Potential Liquidity Impact

The analysis performed in this document quantifies the liquidity impacts due to the downgrade of AIG Inc. The consequences of rating downgrades are the following.

- Threshold and independent amounts: For some contracts, as AIG is downgraded, the thresholds decrease and the independent amounts increase, resulting in additional collateral postings.
- Collateral: Some contracts do not require posting of collateral if AIG is rated above a certain level. Once this level is breached, collateral posting is required.
- Terminations: Counterparties to some contracts have the right to terminate transactions if a rating trigger is breached. The termination is done at a replacement value, which in some cases can be difficult to quantify. Sometimes the rating level is the same as the collateral trigger in which case the counterparty can terminate the trade if collateral is not posted. In other cases, the termination trigger is at a lower level than the collateral trigger.
- Loss of ability to rehypothecate: AIGFP looses the right to rehypothecate collateral received on some derivative transactions below a certain rating level.
- Guarantee/assignment: At some rating level, counterparties to some transactions can require AIG to find a guarantor or a third-party to assign the trades to. In the current market environment we assumed that it would be extremely difficult to find a third party willing to take on these transactions and therefore these triggers were treated as termination triggers for the purpose of the calculation.

In addition there are indirect effects of an AIG rating downgrade:

- Structured transactions: Some securitization vehicles, to which AIG is a derivative counterparty for interest rate or currency risk, have rules that require a minimum rating for the derivative provider. Below a certain rating, the vehicle has the right to terminate the transactions. In that case, any amount owed to AIG on the derivative falls to the bottom of the cash flow waterfall.
- Loss of confidence: In the case of a rating downgrade, counterparties and clients loose confidence and in the worst case there is a run on the bank.

The potential liquidity impact from further downgrades in AIG's credit ratings are shown in the table below:

Summary cash outflows triggered by rating downgrades

USD millions	GICs and CSAs	Multi-sector (see note)	Corporate arbitrage	Regulatory Capital	Total change	Total cumulative
BBB+	3,122	2,833	809	150	**6,913**	**6,913**
BBB	228	2,855	108	600	**3,791**	**10,704**
BBB-	544	0	69	25	**638**	**11,342**
Total	3,894	5,688	986	775	**11,342**	

Important Note:
The multi-sector CDO estimates include at the BBB+ level the effect of the independent amounts and threshold adjustments. They include at the BBB level the effect of the termination of the funded portion of project Max. These numbers do not include the estimate of the replacement cost of trades that terminate for the most part at BBB ($50b of notional out of $70b) because of the uncertainty in the calculation of the replacement cost. As explained in section 2.2, the maximum exposure at the BBB level would be $27 billion.

The remainder of this memorandum explains what these balances represent and additional liquidity effects not quantified in the above table.

2.1. GICs and CSAs

This section covers the potential impact on AIGFP's liquidity resulting from the GIC portfolio and the derivative transaction portfolios (other than credit derivatives).

As of 10/8/08 - obligations at the respective rating levels

USD millions	Cumulative at level			
	GICs	CSAs	Total	*Cumulative Change*
Current level	776	1,716	2,492	
BBB+	896	4,718	5,614	*3,122*
BBB	896	4,946	5,842	*3,350*
BBB-	896	5,490	6,386	*3,894*

Amounts under the GIC column represent the principal amount of GICs that AIGFP would be required either to prepay or to collateralize upon a further downgrade of AIG's ratings.

Amounts under the CSA column represent the following estimates:

- Amount of collateral received by AIGFP under CSAs that AIGFP will no longer be permitted to rehypothecate.
- Estimate of additional collateral postings required of AIGFP.
- Estimate of the mark-to-market value of derivative transactions that are in-the-money to AIGFP's counterparties where the counterparties would be permitted to terminate the transactions and demand mark-to-market payment as a result of a downgrade of AIG's rating. The amounts reflected here are net of collateral already posted to counterparties to secure the related mark-to-market exposures.

Estimates presented below are based on AIGFP's best estimates. Actual liquidity effects may differ from these estimates.

The table below does not take into account the following impacts:

- Estimate of the mark-to-market value of derivative transactions that are in-the-money to AIGFP where the counterparties are permitted to terminate as a result of a downgrade of AIG's rating
- Effect of AIGFP not being able to find a replacement counterparty on derivative transactions where a downgrade of AIG's rating would require such a replacement

Starting with AIG's current rating level, the main impact of further downgrade occurs at the BBB+ level, where \$3.1 billion of additional cash outflows would be triggered. This number includes \$950 million due to the loss of the ability to rehypothecate collateral on some transactions as well as \$820 million of independent amounts that AIGFP would be required to post based on notional amounts of derivative transactions (with supranational counterparties).

2.2. Multi-sector CDOs

In the case of the multi-sector CDO CDS portfolio, further downgrades of AIG's ratings will result in further collateral calls due to decreases in threshold amounts and increases in independent amounts. AIGFP estimates that it would be required to post an additional \$2.9 billion if AIG is downgraded to BBB+. Further downgrades below BBB have no effect on additional collateral requirements.

At the BBB level, the counterparties for trades representing \$50 billion in notional have the right to terminate their transactions. It is very difficult to estimate the replacement cost for these transactions as the market is extremely illiquid on these transactions, and there are no precedents in this area.

As of 10/10/08 - Multi-sector CDO book

USD millions	Current	BBB+	BBB	BBB-	No trigger	Total
Notional	2,342	125	49,883	1,621	16,782	70,753
Collat. Posted	1,281	37	22,517	720	5,876	30,430
Max exposure	1,061	87	27,367	901	10,906	40,322

For purpose of illustration the replacement cost was estimated using the stress prices computed by Blackrock for the Merrill, Goldman and Socgen trades on a transaction by transaction basis. The weighted average of these prices (48.4%) was used for the remainder of the book. Finally, all the prices were stressed down another 15 points, yielding an average termination price for the book of 33.4%.

The additional cash outflow is estimated to be approximately $8.4 billion. This amount corresponds to a termination outflow of $32.9 billion (which impacts the income statement) offset by a return of collateral already posted of $24.4 billion.

Stressing the prices by another 10% would increase the cash outflow by another $5 billion.

As of 10/10/08 - Multi-sector CDO book

USD millions		Current	BBB+	BBB	BBB-
Already posted	30,430				
Additional					
Collateral		(1,281)	2,833	(24,485)	(775)
Termination		1,703	83	32,930	1,080
Net Cash Outflow		422	2,916	8,446	305

Project Max is included in the above numbers for the unfunded portion of the transaction of $2.25 billion to which a portion of the collateral posted ($0.4 billion out of $2.8 billion) was assigned. This trade has a termination trigger at BBB.

The funded portion of $5.3 billion has collateral posted for an amount of $2.4 billion and has also a termination trigger at BBB. As opposed to the derivative trades for which the computation of a replacement cost is necessary, the impact of a downgrade at BBB here is simply the termination of the funding minus the return of the collateral already posted, for a net cash outflow of $2.9 billion. This amount is not included in the tables in this section but is included in the summary table.

The impact at the current level include

- Bank of Montreal trades for a notional of $1.4 billion that AIG FP can terminate at A+ (but not Bank of Montreal) and that have collateral posted for $0.5 billion.
- Start 2005 and Commodore, two positions totaling $0.9 billion in notional that have $0.7 billion of collateral posted. The termination impact was assumed to be the same.

For information purposes, the table below shows at the different rating levels the notional of trades that get terminated as well as the collateral that is already posted against them. The difference between these two amounts is the maximum exposure at each level.

2.3. Corporate arbitrage portfolio

The key liquidity impact from further downgrades of AIG's rating is that at certain levels counterparties will be permitted to terminate transactions at replacement cost. In the case of the corporate arbitrage portfolio, the most significant liquidity impact representing about half of the book requires collateral postings at BBB– and allows the counterparty to terminate the transactions at BBB (approximately $25 billion notional amount).

The collateral requirements were estimated using the most recent prices available (average book price of 97.7%) and terminations were estimated to be done with a 20% increase on the current write-down. For example, if the current price of a trade is 95, the amount used for the collateral estimate is 5 and the cost estimate for the termination of the trade is 5*120% = 6.

The table below shows the effect of these assumptions at the different levels.

As of 9/30/08 - Corporate Arbitage

USD millions		Current	BBB+	BBB	BBB-
Already posted	901				
Additional					
Collateral			588	(645)	(345)
Termination			221	753	414
Net Cash Outflow			809	108	69

The negative amounts represent sums that are returned to AIG FP as transactions are terminated. The last line in the table shows the net cash outflow at each rating level, while the termination line represents the actual impact on the income statement.

2.4. Regulatory Capital Portfolio

In the case of the regulatory capital portfolio, downgrades of AIG's credit rating could trigger either additional collateral calls and/or terminations. In most cases, AIGFP has the right to select either to post collateral or to permit the counterparty to elect to terminate a derivative. Most of the derivative positions that have rating triggers were triggered as a result of the last rating downgrades.

Termination triggers shown here also include the rating triggers where the required action is that AIG must find a qualifying third party to guarantee or to take assignment of the trades. These transactions were included on the assumption that it would be very difficult for AIG to find a third party willing to take on these contracts in the current environment and that the trades would likely be terminated as a result of AIG's failure to do so.

The total population of $249 billion can be broken down in the following categories:

Counterparty - Trade	Notional	Status
Various with rating triggers		
Natixis - Igloo	$2b	Has a termination trigger at A+ but has not called us since the trade terminates in December. Estimate of termination $10m.
ABN - Yellowhammer	$9.2b	Collateral trigger at A-. Estimate is 0 since the calculation is based on expected losses and is deemed to be 0 if there is still a significant AAA tranche.
BNPP GL Liberte 4 and 5	$14.3b	Already posting collateral for a total of $124m. No termination triggers.
Standard – Start 3	$0.7b	Collateral trigger at BBB+. Amount estimated to be 0 because we only start posting when the AAA tranche below us is downgraded, which is unlikely given the performance of the transaction.
Rabobank - Sundial	$2.9b	Collateral trigger at A-, termination trigger at BBB. Estimate for termination: $100m
Dev. Bank of Japan – Cubic1	$2.0b	Collateralization at BBB- or termination at the same level. The cost of collateralization would be $10m as the trade matures in April 2009.
Westpac - Camberra	$1.8b	Collateral trigger at BBB-. Amount estimated to be $15m.
Swedbank - Spintab	$0.7b	Termination trigger at A+. Counterparty indicated that they plan to call the trade as planned in December and not take action based on our downgrade.
Danske – jutland and Private Bricks	$32.1b	Collateral triggers at A-. Already posted $210m
Banco Santander - Hypothecario 3	$1.6b	Collateral trigger at BBB+. We are currently posting collateral for an amount of $413m.
Morgan Stanley - MSCP	$1.1b	Collateral trigger at BBB+ and termination at BBB. Collateral amount estimated to be: $150m Termination costs estimated to be $150m
Northern Rock – Northern Rock	$1.6b	Termination trigger at BBB. Estimate is $500m
Credit Logement	**$33.7b**	**Currently under discussion as these trades have collateral triggers at A+. To be conservative we can assume a collateral amount of $50 million.**
KfW	**$25.9b**	**Collateral posted €200 million. AIG FP is currently renegotiating all the trades with KfW. If this renegociation is successful, this should eliminate any future termination triggers.**
Various with no rating triggers	**$120b**	

Collateral requirements can be in two forms: (i) a mark to market approach that requires the counterparty to find a third-party price for the transaction or (ii) a re-tranching approach, meaning that the collateral posting increases the subordination level back to where it was prior to the downgrade.

The table below shows the cash flow impact at the different rating levels:

As of 9/30/08 - Regulatory Capital

USD millions		Current	BBB+	BBB	BBB-
Already posted	949				
Additional					
Collateral		-	150	(150)	25
Termination		10	-	750	-
Net Cash Outflow		10	150	600	25

APPENDIX

Privileged & Confidential

Draft 10/14/08

Scope of Review of Contracts

- Identify transactions that include contractual provisions that, in light of events occurring in the third quarter of 2008 (including the right of the Federal government to acquire preferred stock convertible into 79.9% of the common shares of AIG, Inc.), would have a material adverse effect on AIG, Inc.'s liquidity position and/or financial condition or results of operations ("Relevant Transactions").

- Examples of such adverse effects, to the extent material to AIG, Inc., include:

  - Additional or unforeseen cash demands
  - Acceleration of obligations
  - Triggering of new or contingent guarantees or other commitments
  - Termination of contracts, rights, authorizations, approvals or permissions

- Examples of the types of contractual provisions that may be relevant to the matters described in the first bullet point above:

  - Change of control provisions
  - Material adverse change provisions
  - Credit rating based provisions

- AIG-FP will undertake the following review process to identify Relevant Transactions, and will utilize the services of outside counsel, as described below, to perform the review.

  ISDA Master Agreements. Weil Gotshal will review ISDA Master Agreements and related Credit Support Annexes (but not trade confirmations) with respect to AIG-FP's derivatives transactions (including transactions with other AIG, Inc. entities) that constitute 90% of the absolute value of mark-to-market exposure, whether of AIG-FP or the counterparties. Weil will also review ISDA Master Agreements and related Credit Support Annexes and trade confirmations for all of AIG-FP's super senior transactions. Cadwalader will review ISDA Master Agreements and related Credit Support Annexes and trade confirmations, as well as related indentures, for all interest rate swaps and other derivatives transactions with CDO vehicles in relation to AIG-FP's super senior transactions. Weil Gotshal will spot check Cadwalader's review of such documentation.

  Muni GIC and Structured Lease Transactions. White & Case and Fulbright prepared and are familiar with documentation regarding AIG-FP's Muni GIC and structured lease transactions. Fulbright previously worked with AIG-FP to develop a detailed database to reflect for all of AIG-FP's Muni GIC transactions, among other items, credit rating based provisions in documentation for Muni GIC transactions. The database was completed in 2005 and has been updated by AIG-FP personnel since then. Fulbright will review documentation for all of AIG-FP's Muni GICs entered into since the date of completion of the database in 2005 and that are uncollateralized to determine whether such documentation includes contractual provisions that are described in the first bullet point above. AIG-FP will also ask Fulbright to confirm, as a general matter, their sense that documentation for Muni GICs entered into before the date of completion of the database in 2005 does not include contractual provisions that are described in the first bullet point above. [In relation to AIG-FP's structured lease transactions, Fulbright and White & Case have already reviewed (i) all of AIG-FP's Equity PUAs and (ii) documentation for all non-Equity PUA roles played by AIG-FP in structured lease transactions for purposes of identifying credit downgrade provisions. Fulbright and White & Case will review the documentation described in clauses (i) and (ii) above for purposes of this broader review] In addition, AIG-FP will meet with the business and legal personnel responsible for AIG-FP's Muni GIC and structured lease transactions to confirm whether they are aware of the inclusion of contractual provisions that are described in the first bullet point above in the documentation regarding such transactions.

BRO Transactions. AIG-FP legal personnel [Jake Sun] will review documentation for at least one BRO transaction with each investment manager with whom AIG-FP has entered into a BRO transaction. In addition, AIG-FP will meet with the business and legal personnel responsible for these transactions to confirm whether they are aware of the inclusion of contractual provisions that are described in the first bullet point above in the documentation regarding such transactions.

Issued Securities. Weil Gotshal will review (i) program documentation regarding AIG-FP's EMTN program (but not AIG, Inc.'s registered MTN program) and pricing supplements regarding issued securities that constitute [90]% of the aggregate notional amount of issued securities issued under AIG-FP's EMTN program and (ii) documentation regarding AIG-FP's (but not AIG, Inc.'s) issued securities that (x) are not issued under a note issuance program, (y) are not issued in relation to a TDG or other structured transaction and (z) constitute [90]% of the aggregate notional amount of issued securities not issued under a note issuance program. In addition, AIG-FP will meet with the business and legal personnel responsible for AIG-FP's issued securities to confirm whether they are aware of the inclusion of contractual provisions that are described in the first bullet point above in documentation for AIG-FP's issued securities.

Repo/Reverse Repo and Securities Lending Transactions. AIG-FP's repo/reverse repo and securities lending transactions generally involve U.S. government and agency, foreign government and corporate debt securities and ABS. AIG-FP legal personnel [Brian Gregory] will review [the form Master Repo documentation for each type of form that is used for AIG-FP's repo/reverse repo transactions and the form Securities Lending documentation for each type of form that is used for AIG-FP's securities lending transactions]. AIG-FP legal personnel [Brian Gregory] will also review Master Repo documentation and Master Securities Lending documentation for AIG-FP's repo/reverse repo and securities lending transactions that, in the aggregate, constitute [75]% of the aggregate notional amount of transactions involving foreign government and corporate debt securities and ABS to which AIG-FP is a party (whether as borrower or lender of securities). In addition, AIG-FP will meet with the business and legal personnel responsible for AIG-FP's repo/reverse repo and securities lending transactions to confirm whether they are aware of (i) the inclusion of contractual provisions that are described in the first bullet point above in documentation for such transactions or (ii) non-standard repo/reverse repo or securities lending transactions (even if documented under Master Repo or Master Securities Lending documentation).

Gold Lease Transactions. AIG-FP legal personnel [Jeff Saxon] will review Master Agreements (to the extent particular gold lease transactions are entered into under Master Agreements) and trade confirmations for all of AIG-FP's gold lease transactions.

TDG, Energy and Infrastructure Investment and Other Structured Transactions. AIG-FP legal personnel (with assistance from outside counsel, as necessary) will review documentation regarding TDG transactions, energy and infrastructure investment transactions and other significant structured transactions (to the extent not covered in the other headings) that AIG-FP has entered into and that are still active. This review will include review of the transactions listed on Ron Latz's liquidity study chart and, for the avoidance of doubt, will include review of AIG-FP's [GAP transactions] and the [Curzon, Nightingale and Horizon transactions]. AIG-FP legal personnel will consider all transactions that have been approved by the AIG-FP TRC or Banque AIG TRC and that are still active for purposes of this review. In the context of reviewing the transactions described in this paragraph, AIG-FP legal personnel (or outside counsel, as the case may be) will consider any guarantees provided by AIG-FP and its subsidiaries in the context of such transactions.

SMBC Credit Agreement. Davis Polk will review the SMBC credit agreement.

Dow Jones/AIG-FP Joint Marketing Agreement. AIG-FP personnel [Jeff Saxon] will review the Dow Jones/AIG-FP joint marketing agreement.

- In response to a prior request from AIG, Inc.'s regulatory and compliance group regarding the effect of an AIG, Inc. change of control on AIG-FP's regulatory licenses and approvals, AIG-FP provided the information attached as Annex I.

- AIG-FP's work product will comprise one or more charts and spreadsheets that are organized in a manner that is similar to information previously provided to AIG, Inc. for purposes of providing information relevant to AIG, Inc.'s liquidity position.

- Any confirmation by AIG-FP personnel will be expressly subject to normal carve-outs, including knowledge, materiality and reasonableness, and will be expressly limited to (i) identifying Relevant Transactions, (ii) AIG-FP performing a documentation review as described in the fourth bullet point above and (iii) AIG-FP providing to AIG, Inc. the work product described in the sixth bullet point above.

Rating Agency Talking Points – October 23, 2008

Rating Triggers

- We are currently undergoing a due diligence process to ensure that we have captured all material transactions that have rating triggers below A-/A3. We expect to be completed in time for the 10Q filing.

- The principal liquidity impacts from further rating downgrades:

  - Additional collateral calls resulting from either (1) threshold levels decreasing or independent amounts increasing, or (2) counterparties becoming eligible to require AIG to post collateral

  - Counterparties receiving the right to terminate trades once a rating level is breached

  - Right for the counterparty to require us to find a guarantor or a replacement counterparty

  - AIGFP losing the right to rehypothecate collateral received on derivative transactions [new]

- Based on the information we have to date, we estimate the impact on liquidity from further rating downgrades as follows:

  - GICs - $120 million relating to residual GICs that either have to be collateralized or paid off

  - Non-GIC portfolio (excluding credit derivative portfolio)

    - Approximately $950 million related to the loss of the right to rehypothecate collateral received
    - Approximately $2 billion at BBB+ / Baa1 related to either additional collateral posting requirements or estimated impact of terminating trades that are in the money to the counterparty. This amount grows to $2.8 billion at the BBB- / Baa3 level.

  - Multi-sector CDO portfolio

    - At BBB+, we estimate that we will have to post an additional $2.9 billion in collateral relating to changes in threshold levels and independent amounts. No further adjustments below this level.
    - At BBB, counterparties on approximately $50 billion in notional exposure are able to terminate the trades at their replacement cost.

We have posted approximately \$22.5 billion in collateral against these trades (before considering the additional \$2.9 billion in collateral from being downgraded to BBB+). So the liquidity impact will be the difference between the replacement cost of these transactions and the collateral already posted.

- At this time, we have posted collateral equal to the mid-market prices that we have agreed to with our counterparties, leaving an uncollateralized notional amount on these trades of approximately \$27 billion.
- It is difficult to reasonably estimate the replacement cost given the lack of trading and price transparency in this asset class.
- As an example, every 10 point difference from the mid-market prices is approximately \$5 billion.

- Also at BBB / Baa2, one of the repo facilities on 2a7 becomes due and payable.

- Regulatory Capital CDS

  - Most trades that had a rating trigger were triggered when AIG was downgraded to A-/A3
    - In these cases, we had the choice of posting collateral, finding a guarantor / assignor, or allowing the counterparty to terminate. In all of these cases, we had opted to post collateral. The amount of collateral posted was or will be approximately \$600 million.
  - If downgraded below A-/A3, 4 additional trades get triggered, which is not expected to have a material effect.

- Corporate Arbitrage

  - Trigger for additional collateral at BBB+
  - Rights to terminate \$25 billion at BBB / Baa2

PRELIMINARY DRAFT

595

Project Independence

Illustrative Recovery Analysis

24 October 2008

PRELIMINARY DRAFT

[redacted]

Illustrative Recovery Analysis

Assuming $85Bn FRB Loan

- Table at right shows illustrative recoveries for FRB under alternative structures in different scenarios
- Generally speaking, net cash proceeds from sales of businesses are likely to be higher assuming stable ratings (i.e., alternative C) than in downgrade or bankruptcy scenarios
- Given the multiplicity of factors that could influence results, including business performance and the behavior of customers, employees, distributors and competitors, it is very difficult to predict the actual cash proceeds that would be realized in each case
- In addition, actual cash proceeds realized and recoveries by FRB will also depend upon a number of other factors, such as:
  - Overall economic environment
  - State of financial markets generally
  - Business and financial position, including ability to obtain financing, of potential acquirers of AIG businesses
  - Actions by insurance and other regulators

	Alternative A	Alternative B	Alternative C
Description	• Maintain $85Bn FRB senior secured facility with current rate and tenor	• Maintain $85Bn FRB senior secure facility • Restructure maturity and rate • Implement ML II & ML III	• Restructure FRB facility to be $45Bn senior secured, $40Bn subordinated • Restructure maturity and rate • Implement ML II & ML III
Key Assumptions	• Immediate downgrade to BBB or lower • Liquidity need of at least $42Bn • Company files for bankruptcy	• Immediate downgrade to BBB • Liquidity need of $10Bn related to FP (non-CDO portfolio) • Continue as going concern	• Maintain current ratings • Continue as going concern
FRB Repayment ($Bn) **Total Net Cash**			
$118 [1]	$85	$85	$85 ← AIG Management Case
110	85	85	85
95	85	85	73
80	80	70	62
65	65	55	50
50	50	40	45
Additional Considerations	• Difficult to quantify impact on proceeds due to HoldCo bankruptcy filling, likely seizures of insurance companies by state regulators • Potential significant systemic effects of bankruptcy on financial markets	• Incremental liquidity needs and impact on AIG businesses resulting from downgrade are difficult to assess • Potential for subsequent downgrades • Does not reflect potential cost to FRB of ML II and ML III	• Assumes subordinated portion is junior to senior unsecured debt and hybrids, but does not reflect other potential unsecured claims, which could be material • Does not reflect potential tax implications of FRB facility restructuring • Does not reflect potential cost to FRB of ML II and ML III

Note
1. Management Case: includes $83Bn of proceeds from planned asset sales, $27Bn net value of target core and $8Bn other cash flow through 2010

Illustrative Recovery Analysis

Assuming $100Bn FRB Loan

- Table at right shows illustrative recoveries for FRB under alternative structures in different scenarios
- Generally speaking, net cash proceeds from sales of businesses are likely to be higher assuming stable ratings (i.e., alternative C) than in downgrade or bankruptcy scenarios
- Given the multiplicity of factors that could influence results, including business performance and the behavior of customers, employees, distributors and competitors, it is very difficult to predict the actual cash proceeds that would be realized in each case
- In addition, actual cash proceeds realized and recoveries by FRB will also depend upon a number of other factors, such as:
  - Overall economic environment
  - State of financial markets generally
  - Business and financial position, including ability to obtain financing, of potential acquirers of AIG businesses
  - Actions by insurance and other regulators

	Alternative A	Alternative B	Alternative C
Description	• Maintain $85Bn FRB senior secured facility with current rate and tenor • Assumes additional $15Bn senior secured FRB loan required for liquidity needs	• Maintain $85Bn FRB senior secure facility • Assumes additional $15Bn senior secured FRB loan required for liquidity needs • Restructure maturity and rate • Implement ML II & ML III	• Restructure FRB facility to be $45Bn senior secured, $40Bn subordinated • Assumes additional $15Bn senior secured FRB loan required for liquidity needs • Restructure maturity and rate • Implement ML II & ML III
Key Assumptions	• Immediate downgrade to BBB or lower • Liquidity need of at least $42Bn • Company files for bankruptcy	• Immediate downgrade to BBB • Liquidity need of $10Bn related to FP (non-CDO portfolio) • Continue as going concern	• Maintain current ratings • Continue as going concern
FRB Repayment ($Bn) **Total Net Cash**			
$118 (1)	$100	$100	$91 ← AIG Management Case
110	100	100	85
95	95	85	73
80	80	70	62
65	65	55	60
50	50	40	50
Additional Considerations	• Difficult to quantify impact on proceeds due to HoldCo bankruptcy filling, likely seizures of insurance companies by state regulators • Potential significant systemic effects of bankruptcy on financial markets	• Incremental liquidity needs and impact on AIG businesses resulting from downgrade are difficult to assess • Potential for subsequent downgrades • Does not reflect potential cost to FRB of ML II and ML III	• Assumes subordinated portion is junior to senior unsecured debt and hybrids, but does not reflect other potential unsecured claims, which could be material • Does not reflect potential tax implications of FRB facility restructuring • Does not reflect potential cost to FRB of ML II and ML III

Note

1. Management Case: includes $83Bn of proceeds from planned asset sales, $27Bn net value of target core and $8Bn other cash flow through 2010

Rating Agency Strategy

Objective: Mitigate risk of rating agency downgrade; maximize window to react to a downgrade if inevitable
Mitigate impact of 3Q earnings on rating agencies, investors, market

Risks: Rating agencies downgrade regardless of actions taken; agencies do not understand actions taken
Market/investors/employee reactions extreme

Earnings: 3Q losses (a multiple of expectations) much higher than expected

Downgrade Impact At BBB: Downgrade impact comes in primarily two forms: liquidity demands at HoldCo and impact on operating subs' operations

1. HoldCo liquidity and cash flow impact on unregulated entities
   $7.2B in collateral calls (CDS)
   $5B to $33B in termination costs (CDS)
   $1B to $3B (reg. cap. arb.)
   +/- $1B (corp. arb.)

2. Impact on operating subs' operations
   (a) valuation impact on assets to be disposed – depends on ratings impact at the OpCo level
   (b) negative impact could be mitigated if OpCo ratings are maintained by allowing greater notching between HoldCo and OpCo ratings

Recommendation:

1. Rating agency "holiday" – two-month stay of ratings actions (not likely to happen); we want the rating agencies to keep AIG in the penalty box (instead of being downgraded) until the broader economic issues "stabilize" and AIG, with its unique circumstances, can be compared to peers; issue is that maintaining our flexibility to "walk" on the options would compromise our credibility if exercised.
2. Iterate with rating agencies on package of mitigants to provide input to ratings decision process
   a. If no information is provided, agencies likely to pull trigger (gave AIG/FRBNY two weeks to iterate prior to investor call on 10/3)
3. Start sooner rather than later – week of October 12
   a. Discussing solutions in advance will provide us information on the structure of the solutions and whether the agencies believe that the structures address the core issues of the firm
   b. Will potentially give us more time to address agencies' issues
   c. Work with the agencies on ML 2 and be prepared to begin discussions of ML 3; key issue will be our confidence in pursuing these paths
4. Consider timing of execution of solutions
   a. How long do we wait to execute on solutions?
   b. Do we keep solutions as "last" alternative – but ready to execute?

c. Do we execute early to signal willingness/efforts to stabilize firm?

Message to rating agencies:

- Things have fundamentally changed; we are committed to (market stability and) stabilizing company to provide time to execute orderly disposition process, maintain franchise value, and pay back U.S. taxpayers
- We have worked with company to develop solutions to two largest problems in the company (Securities Lending and FP)
  - Demonstrated action with Securities Lending Program
- We have additional solutions to more permanently address SL and FP
  - We want your feedback on these solutions to get them "right"
- We are committed to maintaining financial strength at the operating subsidiaries in order to support franchise value and avoid potential deterioration
  - ML2 will resolve issues in the RMBS portfolio, giving cash to the insurance subsidiaries
  - Plan to convert HoldCo loan to selected insurance subsidiaries into surplus, thus improving capital adequacy

On a separate but linked track:

- Consider asking rating agencies what they are valuing in this economic environment; they are under enormous pressure to get it right this time and may find value in discussion of the broader economy with other smart people. This would facilitate everyone having better information.

Week of:	Company Actions	FRBNY Actions
October 13	▪ 10Q drafting ▪ Audit Committee Meeting	▪ Discuss ML 2 with firm ▪ Open discussions with rating agencies on broader strategy; provide details on ML 2 ▪ Solicit feedback, adjust recommended ML 2 options ▪
October 20	▪ Press release drafting ▪ Audit Committee review of 10Q ▪ Business unit analyses conclude	▪ Discuss broad aspects of FP solutions; provide some thinking on ML 3 structure ▪ Solicit feedback, adjust ML options ▪ Discuss aspects of
October 27	▪ PWC Concludes ▪ Final Audit Committee meeting ▪ Rating agency discussions on 3Q earnings ▪ **File 10Q on 10/30** ▪ Investor call on 10/31	▪ TFG meets with rating agency CEOs ▪

Materials for 4pm meeting on ML III

Amy Flynn

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o
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Timothy Geithner, Thomas Baxter, Terrence Checki, Christine Cumming, Michael Silva, Meg McConnell, Paul Whynott, Jim Mahoney, Steven.Manzari, Amy Flynn

10/26/2008 03.34 PM

Show Details

Please find attached materials for the 4pm meeting to discuss Maiden Lane III. * * *Amy FlynnFederal Reserve Bank of New YorkOffice: 212-720-6431Cell: 347-266-4820 - Slides for MS on MLIII 10-26-08.ppt - 2008-10-25 MLNE III Structure v2.ppt

AIG FP SYSTEMIC RISK ANALYSIS – DRAFT

Ref	Issue	Accnt	Description	Systemic Risk (H/M/L)	Who is the likely counterparty to these transactions	Risk to Counterparty of AIG-FP failure	Risk to AIG	Further Research
	LIABILITIES							
1.1	**FP Intercompany Payables**		Funds lent from parent and intercompany transactions between FP and other AIG companies. Estimate $54 bil due to parent AIG ; $1.85bil due to other AIG entities much of which without collateral	**High** – Failure of FP to perform on obligations to other AIG entities may create event of default for the company.	Parent company and other AIG subsidiaries.	Failure of FP may put at risk the financial condition of other AIG operating entities	**High** – FP's inability to repay loan to Parent may cause AIG failure	Unclear level of subordination to other payables
1.2	**Banque AIG**		A significant face to customers of AIGFP. Regulated banking vehicle in France. All of the risk is back-to-back with AIGFP AIG has pledged to support Banque AIG and AIG generally provide guarantee under CSA..	**High** should FP failure lead to Banque AIG failure with systemic transmission of losses to counterparties.	Banque AIG is face to Reg Cap Arb counterparties and other derivative products of FP in the European market. Currently, Due from AIG FP is approximately $300 mil.	Banque AIG becomes highly risky due to unhedged net open positions	**High** -Risk of preemptive action by the French on Banque AIG regulators. Guarantees could be a liquidity drain	- What is the position of the French bank relalatory authorities regarding Banque AIG?
1.3	**Medium Term Note, Private Placements and Curzon**	0332	$19 bil of generally unsecured borrowings include; Curzon ($4.6 bil), EMTNs ($3.9 bil) US MTN ($1 bil), Private Placement ($13.6 bil) include Commodity linked, credit linked, zero coupon, PRD, equity linked notes. The majority of bonds are in USD, EUR, JPY. Some bonds are puttable and some have accelerated trigger events	**High** Potential unexpected loss of principal on principal protected notes	Sold to regional banks and institutional investors with some ultimate distribution to high net worth investors.	Loss of principal and interest upon default	**Low**	Clarify risk of loss by end investors Confirm if off AIG shelf
1.4	**Project Max**	TBD	2a7 liquidity puts – secured loan from Deutsche Bank backed by CDO collateral. 3 year roll period. $5 bil to $7.5bil.	**Moderate – Low** Single counterparty, collateralized risk	Deutsche Bank	Secured loan Loss of principal and interest upon default	**Low**	
1.5	**Solar Funding**	0285	A secured loan from RBS backed by RMBS and other assets (approximately $2 bil.	**Moderate – Low** Single counterparty, collateralized risk	RBS	Secured Loss of principal and interest upon default	**Low**	
1.6	**Emerald (ETF Notes)**	0310	Commodity ETFs sold to high net worth individuals (approximately $2 bil)	**Moderate** - for Exchange Traded Fund ($2bn) where retail investors invested in these ETF trades will be terminated. Retail investors can terminate anytime and AIG-FP needs to repay in the next 3 days	High net worth investors	Loss of principal and interest upon default (depending upon security)	**Low**	Clarify risk of loss by end investors. Delisting activity
1.7	**Darts (MTN)**	0331	Equity linked notes sold to regional banks and institutional investors ($1.1 bil).	**Moderate**	Sold to regional banks and institutional investors with some ultimate distribution to high net worth investors	Loss of principal and interest upon default	**Low**	Clarify risk of loss by end investors
1.8	**GICs**	0344	Collateralized - $9.7 bil Uncollateralized - $1.7 bil	**Low to Moderate**	Various counterparties - including municipals	Predominately secured	**Low**	
1.9	**Gold Leases**	0346	$1.7 bil largely with central banks.	**Moderate**	Central Banks	Secured and unsecured	**Low**	Follow up on deal specifics
1.10	**Nightingale SIV**	0077, 0348	AIGFP holds $1.6bil in senior notes issued from busted SIV whose assets are largely RMBS and Corporates. Capital notes are deep under water.	**Moderate**	Institutional Investors (primarily Asian and European) - 17 counterparties who have Capital Note exposures. Capital role holders have written off majority of the value already.		**High** – as it converges with the concentrated credit risk of the entity Standard market and credit risks.	
1.11	**Repos**	TBD	Total balance $12 bil includes: 3rd party Repos: $4 bil Portfolio Swaps: $2 bil AIG Repos (to parent) $6 bil	**Low**			**Low**	
	DERIVATIVES							
2.1	**Derivative Payable**	0077, 0318	Derivative unrealized losses due to counterparties	**High**	Counterparties include nationals, supra nationals, SPVs, corporates, and financial institutions Net unrealized gain/loss ($bil). Gross unrealized gains 17 Collateral received (6) Net unrealized gain 11	- Unsecured exposure for amount in excess of collateral - Counterparty would need to replace position in the market. - Generally, corporate	**N/A**	

Note: All derivatives are mid market and exclude replacement costs (as of dates 9/23 – 10/10)

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AIG FP SYSTEMIC RISK ANALYSIS – DRAFT

Ref	Issue	Accnt	Description	Systemic Risk (H/M/L)	Who is the likely counterparty to these transactions	Risk to Counterparty of AIG-FP failure	Risk to AIG	Further Research
					Gross unrealized loss 46 Collateral posted (38) Net unrealized loss 8 Total net unrealized gain 3 See Top 50 Unrealized Loss Report excluding intercompany (Attached).	counterparties and SPVs do not post or receive collateral.		
2.2	**Regulatory Capital Arbitrage Trades**	0077, 0348	Short protection on $240bil of assets on balance sheets of European Banks	**High** – currently provides estimated $11.1bil of regulatory capital relief to European banks operating under Basel I.	25 European Banks and one issuance vehicle. Including largest counterparties (loan balance insured): ABN AMRO $56 bil Credit Logement $34 bil Danske $32 bil KFW $30 bil	- Currently providing $11bil in capital relief in European Banks at time of global financial crisis. - Replace cost on early termination. - Market access for these trades in current environment. - Tie to termination analysis	**High** 1>European recession creates potentially material losses. 2>Bank regulators and/or counterparties require collateral to support performance – creating liquidity drain. 3>Trades must be marked-to-market due to increasing economic risk and derivative form (eg. Santander). 4>Replacement costs on early termination.	Obtain approval memos and confirms. Assess likelihood of Risks to AIG.
2.3	**Multi-Sector CDS on CDO**	0077, 0348	Protection written on $72B of mostly sub-prime CDOs. No hedges.	**High to AIG** – Impact on AIG continued capital and liquidity losses potentially leading to bankruptcy of AIG and further destabilization of the financial markets. This comes after FRB already provided $123bil of liquidity to AIG. **Moderate to Counterparties**– Impact on counterparties given level of collateralization.	US and European bank and investment Banks. Goldman Sachs largest counterparties are, Societe Generale, Deutsche Bank, Merrill Lynch and Calyon. Full collateralization mitigates the impact of FP failure. ($31 bil posted against mark of $33 bil).	Collateral at current market mitigates much of potential loss on FP failure. Clients would have unhedged net open risk after a default.	**High** Mark-to-market losses of $34bil have impaired earnings and capital. Cash flow and liquidity is impaired due to collateralization.	
2.4	**Interest Rate Derivative and Bermudan Swap**	0077, 0348	Long dated and exotic interest rate derivative book – some with maturities up to 70 years.	**Moderate to High** Counterparties are financial institutions, many of which are SPVs (mainly CDOs) that issued securitized assets whereby AIG-FP has provided the wrapped interest rate hedge/swaps. The SPV's consequence requires immediate replacement (cannot take the risk) or unwind the SPVs. Unwind would create systemic market risk esp in the housing market. However, they are likely to replace the hedge at a higher hedging cost	Financial institutions and roughly 130 domestic SPVs	Financial institutions have collateral, exposure and replacement. Some SPV counterparties have large uncollateralized derivatives mark to market including Granite Master (Northern Rock SPV $0.6B) and Aire Valley (HBOS SPV - $0.3B)	**Moderate** but challenging. Large net open loans volatility risks in long term Bermudan swaps: EUR vol $65mm, GBP vol $35mm, USD vol $25mm	SPV due to and due from exposure
2.5	**AIG Intercompany Derivatives**	0280	Unrealized losses on derivatives to AIG entities – total FP due to Other AIG subsidiaries estimated at $1.85bil	**Potentially High** depending on loss transmission via intercompany linkages - Replacement costs - Uncollateralized exposures	AIG insurance subs, Financing subs - AGF, ILFC, others TBD. - ILFC 695.2 - AIG MIP 441.5 - SunAmerica LIC 240.3 - Amer General 225.4 - AISLIC 81.6 - ALIC (Del) 63.6 - AIG Sun ALAC 40.6	Failure of FP may put at risk the financial condition of other AIG operating entities	**High** Risk of preemptive action by regulators (insurance) to collateralize, secure or terminate exposures. Similar risk at point of sale.	- Need to map out intercompany guarantees and other covenants that would transmit an event of default to other AIG entities. - Other intercompany balances (non-derivatives)

Note: All derivatives are mid market and exclude replacement costs (as of dates 9/23 – 10/10)

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AIG FP SYSTEMIC RISK ANALYSIS – DRAFT

Ref	Issue	Accnt	Description	Systemic Risk (H/M/L)	Who is the likely counterparty to these transactions	Risk to Counterparty of AIG-FP failure	Risk to AIG	Further Research
					- ALIC (Ldn) 26.8 - AIRC 21.8 - AIG Pvt Bank (Zur) 17.7			
2.6	**Stable Value Guaranty written on Pensions**	0077, 0348	Stable Value Guarantees (SVG) written on 186 pension plans with total market value of $35.7bil. Contingent liability for FP as the Stable Value Guaranty exceeds the Market Value of the assets by roughly $1.6bil. Risk for FP mitigated by actuarial likelihood of withdrawal. Risk for pension beneficiaries is loss of $1.6bil.	**High** – given the potential loss of $1.6bil in pension assets should FP fail. However, it may be possible to assign the wraps to other 3rd party providers. There are about 10 players in the market that could be approached for assignment.	Counterparties are the trusteesof stable funds in 401k plans and beneficiaries are the participants of the 401k plans. Total counterparties of 186. Largest counterparty is $3 bil. The Pension Plan is at risk of loss if the contracts are not reassigned prior to FP failure.	Failure of FP may create material losses to SVG counterparty. Impact of FP failure on pension provider and pension plan beneficiaries must occur with BV to MV deficit and qualified redemptions. Terminations occurring voluntarily and UBS exiting business.	**Moderate (consider Low)** – potentially high. Current liability is roughly $1.6bil (excess book value over market value). Current market conditions likely to increase this liability. For realized, must be simultaneously book to market value shortfall and sizeable qualified redemptions. Actuarial modeling of loss (due to qualified events of withdrawal) needs to be updated to determine likelihood of loss recognition on AIG books.	What happens to the Plan at default?
2.7	**Power Reverse Dual (PRD)**	0077, 0348	Long Term Structured Notes issued to Japanese retail through Japanese Financial Intermediaries. Structure: 364 swap trades with embedded currency options. $5B notional and $285M market value. Maturities between 10 years and 30 years. Issuers of the note in many cases are supranationals, European banks and other major financial institutions – including AIG. Generally, the options are in the money options, particularly the AUD/JPY deals. Many other dealers have written PRD notes and therefore have similar positions to AIG => capacity to sell/transfer the book may be constrained.	**Moderate (consider High)** risk is limited to issuing banks having to replace PRD swaps which are not liquid in the current market and hence at a higher cost. AIG-FP is the swap counterparties to the Issuing Banks (mainly European financial institutions as they required good ratings). These bonds are then sold on to the Japanese investors via Japanese retail banks/brokers Underlying bond investors are not directly effected as they would still hold the underlying note.	58 counterparties in total Mainly Bond Issuers (IBRD, Supra National) within PRD structure - European banks including Nederlandse Waterschapsbank, KFW, BNP, Dexia Others include Goldman Sachs, IBRD, EBRD, TD Toronto	Issuing banks (mainly European and Japanese-highly rated banks) will lose their hedges, some are positively marked and some are negatively marked. Some counterparties have very large uncollateralized exposures to FP on these deals. Given the liquidity in the market, unlikely for the Issuing banks to recall the PRD bonds and more likely to replace the hedges at a relative significant cost to the issuing banks	**High** Long term complex optionality in currencies and rates. Un-hedgeable of FX skew risk, cross gamma risk, correlation risk (IR/FX), PRD skew No likely buyers of these trades in the market	
2.8	**Municipal Swaps**	0077, 0348	$2.56bil of swaps with Municipalities to transform fixed rate tax-exempt debt to short term paper that may be distributed to tax-exempt 2a7 funds in the form of Variable Rate Demand Bonds (VRDBs).	**High** – Positions are all in-the-money for AIG-FP so counter parties have a replacement cost buffer. Failure of FP as the swap counterparty may disrupt the capacity of the Municipality to fund itself by the VRDB structure. Mitigant is the potential to find another dealer to step in to the swap.	Total swaps of 23 municipal authorities issuing fixed rate debt that AIG swaps to short term. Currently there are 14 swaps based on bond rates, the rest have either terminated or converted to Libor or SIFMA based which are more easily replaced. SCCPA ($266 mil) and Clark County ($124 mil) have the highest bond rate notionals.	Currently negotiations to unwind of $1.1 bil.	**Low** Excluding SIFMA or Libor floaters, AIG pays rate set by remarketing agent for VRDBs. Investors have put the bonds back to liquidity provider causing rate to set high. Tax basis risk in swap. P/L from bond fixing $-12mm this year. MTM for the swaps are positive because current rates are lower than 1990's when the swaps were entered.	
2.9	**Hedge Fund**	0077,	Constant Proportion Portfolio Insurance (CPPI)	**Moderate**	Investors in CPPI notes issued by	Failure may leave	**Moderate** but likely.	Who are the investors in

Note: All derivatives are mid market and exclude replacement costs (as of dates 9/23 – 10/10)

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AIG FP SYSTEMIC RISK ANALYSIS - DRAFT

Ref	Issue	Accnt	Description	Systemic Risk (H/M/L)	Who is the likely counterparty to these transactions	Risk to Counterparty of AIG-FP failure	Risk to AIG	Further Research
	Derivative	0348	principal protected structured notes linked to Hedge Fund (HF) and Fund of Hedge Funds (FOHF) returns. AIGFP has issued CPPI notes directly – and also provided loss insurance to other CPPI issuers on the Gap Risk embedded in the product. CPPI gap risk is the risk that a CPPI issuer is unable to sell the HF or FOHF investment fast enough and buy the zero coupon bond that ensures principal repayment in the event the HF or FOHF loses value quickly. FP loss if all HF/FOHF values go to zero is $2.6bil.	Investors in AIG issued CPPI notes face loss of principal on FP failure. Counterparties to Gap Risk Insurance sold lose value of insurance.	AIG include institutional investors such as Vienna Life and Bayer. Counterparties on Gap Risk Insurance sold by AIG are other CPPI sellers which are largely sophisticated financial institutions	investors in AIGFP CPPI notes unsecured creditors in bankruptcy. Gap risk insurance buyers left open upon FP failure subject to collateral.	Current market unwind of CPPI creates likelihood of loss on gap risk in CPPI and the insurance sold on gap risk in CPPI. Potential loss should all NAV go to zero is $2.6bil. Of this $1.1bil is driven by trades formerly backed by Lehman which are now unhedged and is in the process of exiting align with the 6-9 months gating restrictions imposed.	CPPI notes?
2.10	**Equity Derivative (ex Austria)**	0077, 0348	300 structured trades. $8bil in total.. More complex trades include multi-factor optionality and path dependency.	**Moderate** – AIG-FP provides hedges to Equity Linked Notes issued by other financial institutions. The note issuers will need to find hedge replacement upon AIG-FP defaults	All financial institutions except one counterparty with Enresa which is a Spanish nuclear decommissioning fund.	Most financial institutions' exposures are net of collateral. Financial institutions will have replacement risk/cost.	**Moderate** but challenging. Risk managing a large complex OTC equity derivative book with multifactor optionality in volatile market	Getting further info on counterparty names and rationale for trades
2.11	**Interest Rate Derivative and Bermudan Swap - LOBOs**		GBP Bermudan Lenders Option Borrowers Options "LOBO" cancellable swaps up to 70 years (over $1bn notional) Provides hedges to European Banks	**Low to Moderate** Swap to institution parties have funded UK Local councils /authorities that have structured step funding from European banks (namely Dexia).	Dexia and other European banks	The lenders, European banks hedge the coupon with AIG via LOBOs swaps, The issuing banks would lose the value in the hedges (mitigated by collateral) and need to replace the swap.	**Moderate** The swaps are fairly illiquid considering currently market conditions and could estimated cost $30-40m to liquidate. Difficult to manage the P&L risk and requires rebalancing of hedges Some similar risk profiles to PRDs apart from FX/ IRR correlation.	
2.12	**Mutual Fund Derivatives.**	0077, 0348	Constant Proportion Portfolio Insurance (CPPI) – principal protected structured notes linked to Mutual Fund returns. Amount issued is $406mm	**Low**	Retail mutual funds primarily in the European markets. Very retail focused.	Failure may leave investors in AIGFP CPPI notes unsecured creditors in bankruptcy. Gap risk insurance buyers left open upon FP failure subject to collateral	**Low** Current bear market increases likelihood of loss on CPPI and Gap Risk written	Who are the investors in CPPI notes? Retail mutual funds primarily
2.13	**Stable Value Guaranty written on Bank Owned Life Insurance (BOLI)**	0077, 0348	Stable Value Guarantees (SVG) on $4bil of Bank Owned Life Insurance (BOLI). Risk to FP is coincidence of Market Value less than Stable Value Guaranty combined with actuarial event causing withdrawal (mortality of the insured population)	**Low** – the book value market value differential is estimated at $40mm (ie. 1% of assets).	Counterparties are 4 carriers (Hartford Life, Metlife, Transamerica, MassMutual) and policy holders are JP Morgan Chase and Bank of New York (Mellon).	Failure of FP may create material losses to insurance policyholder. Loss of SVG creates potentially large market value risk and income volatility to insurance purchaser.	**Moderate** – currently. Further losses in MV could drive loss recognition in AIG and potential collateral requirements	
2.14	**Credit Gap Risk Insurance Trades**	0077, 0348	This is gap risk protection sold to banks as a hedge over their Gap Risk obligations to Credit CPPI structures. Exposure fluctuates greatly depending on "reserve" level and "leverage multiple". Varies from approximately $500m to $2.5B under current market conditions.	**Low** Unlikely that the likelihood and magnitude of gap risk losses protected by AIG will make a difference to circumstances if market gaps	The counterparties to these are investment banks (ABN AMRO and Deutsche), however no obligation to the note holders	Gap risk insurance buyers left open upon FP failure subject to collateral	**Moderate.** Current bear market increases likelihood of loss on CPPI and Gap Risk written	

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Note: All derivatives are mid market and exclude replacement costs (as of dates 9/23 – 10/10)

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2.15	**Republic of Italy Trades**	0077, 0348	Structured derivatives with Republic of Italy roughly $671mm of market value. AIG downgrade motivates termination with replacement costs. 1>CMS swap EUR1bil expiry 2019. 2>Zero/Par swap EUR1bil expiry 2033 3>Cash flow/libor swap EUR2.43bil expiry 2024	**Low** –Republic of Italy is deeply out of the money. CS showing interest to step into trade.	Republic of Italy (ROI) uses these trades to hedge their funding.	Replacement costs of trade.	**Low** AIG potentially will suffer adverse termination price due to downgrade. Looking to novate them to Credit Suisse at $75m-$100m liquidation loss, but current MTM is $673m	
2.16	**Equity Derivative / Austrian Trades**	0077, 0348	Short long term (expiry 2013) equity put options on Austrian equities. AIG option to convert underlying reference variable to eurostoxx 50.	**Low** – AIGFP currently in unrealized gain of $100million. Active novation discussions	Two Counterparties – Wuestenrot and Wiener, which are both pension plans.	Counterparty currently out of the money	**Moderate** Short 30 year puts on Austrian equities with no offsetting hedge. Can convert reference to eurostoxx 50.	Confirm termination provision
2.17	**Commodity Books**	0077, 0348	$7.5bil notional in commodity swaps and other derivatives	**Low** – depending on the counterparties	Main counterparties are Barclays and Exchange Traded Funds (ETF). Liquid underlying so replacement cost is relatively low.	FP failure results in unhedged exposures or lack of commodity exposure otherwise provided by FP.	**Moderate** Should be capable of being unwound in orderly manner	
2.18	**Corporate Arbitrage Books**	0077, 0348	$52bil of super senior CDOs . High concentration in financial service.	**Low** – unless losses become material	Banks in all cases	Collateral posted Currently little collateral posted; however, replacement costs would be very high in current market	**High** Standard market and credit risks of a $52bil portfolio of CDOs in credit bear market.	
2.19	**Mezzanine and Single Name CDS**	0077, 0348	Mezz book long $3.785bil against $.98bil short. Single name cds $3.2bil notional	**Low**	Mainly banking counterparties (largest for AIG sold protection: Danske (2.8bn) and for purchased Curzon ($0.7bn) Bayerische and Hexahome ($0.4bn each).	Currently little collateral posted; however, replacement costs would be very high in current market.	**High** – as it converges with the concentrated credit risk of the entity Standard market and credit risks…	
	ASSETS							
3.1	**Assets Held For Sale Portfolio**	0057	$51bil in securities held as AHFS - $17bil of which are reported to be unencumbered.	**Low**	N/A - Security	N/A	**Moderate** – there seems to be difficulty in selling position of marks	
3.2	**Infrastructure Trades and Strategic Investments**	0080	Variety of Private Equity infrastructure deals and tax enhancement trades totaling $820mm Includes: (at 6/30 or 8/31?) Tenaska Marketing $300 mil GS Infrastructure Ptrs $234 mil Stanton Wind Farm $102 mil Other (Deutche Bank) $1.4 bil Leveraged leases $176 mil	**Low**	**N/A** - Security	**N/A**	**Low** – with exception for contingent liquidity draw of $1bil on AIG in Tenaska deal.	
3.3	**Short term investments**	0045	Includes investments with AIG-IC. Balance at 8/31 was $1.4 bil. The account represents AIGFP's participation in Sec lending arrangements with other AIG entities.	**Low**	**N/A**	**N/A**	**Low**	
3.4	**Trade receivables**	0072	Receivables at 8/31 was $9.8 bil. Includes: collateral posted, A/R, stock borrowed, due from brokers, fails to deliver and margin deposits. Payables at 8/31 was $3.1 bil and includes: collateral received, A/P, due to brokers, fails to receive and customer margins/T-bills.	**Low**	**N/A**	**N/A**	**Low**	
3.5	**Investment in partially-owned companies**	0090	Balance at 8/31 was $4.7 bil includes an investment in Bermuda Life.	**Low**	**N/A**	**N/A**	**Low**	
3.6	**Current tax receivable (payable) – AIG**	0192	Balance at 8/31 was $9.4 bil	**Low**	**N/A**	**N/A**	**Low**	

Note: All derivatives are mid market and exclude replacement costs (as of dates 9/23 – 10/10)

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AIG FP SYSTEMIC RISK ANALYSIS – DRAFT

Ref	Issue Parent	Acent	Description	Systemic Risk (H/M/L)	Who is the likely counterparty to these transactions	Risk to Counterparty of AIG-FP failure	Risk to AIG	Further Research

Risk Criteria Legend: *The following criteria were used to determine whether the risk was High Moderate or Low*

Systemic Risk	- the size of the exposure relative to the market overall (e.g. absolute size of the exposure) - the size of the exposure relative to the other AIG entities (e.g. intercompany activities can the event impact AIG Inc. which is viewed as a systemic event) -the size of the counterparty (e.g. size of the exposure relative to the counterparty and its ability to absorb loss) - the nature of the counterparty (e.g. derivatives dealer vs. pension plan/individual investor) - the systemic importance of the counterparty (e.g. impact upon counterparty related to broader impact upon market stability)
FP Risk to AIG	- the size of the exposure relative to the capital, liquidity and risk position of FP.

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Note: All derivatives are mid market and exclude replacement costs (as of dates 9/23 – 10/10)

Potential Implications of AIG-FP failure

1. **AIG-FP Presents Substantial Risk to AIG Inc and Other AIG Subsidiaries:**
   - **AIG-FP (FP) contains substantial market and credit risks**:
     - Long $414bil in credit risk in CDS and bonds
       - $71bil long super senior tranches of mostly subprime CDOs via CDS
         - $34bil in losses impairing earnings, capital and liquidity (due to collateral posted)
         - $7bil additional collateral required at downgrade to BBB+
         - Counterparties obtain rights to terminate trades at BBB
       - $52bil long Corporate and Financial Institution credits via CDS
       - $240bil long European Corporate and Mortgage credit via CDS (reg cap arb trades)
       - $51bil long cash securities in ABS, CLO, CDO, Corporate and Agency debt
     - Short gap risk in Hedge Funds and Credit - $4.6bil reference notional
     - $2tril notional derivative book with 33,000 trades including long term, complex, multi-factor optionality in equities, currencies, interest rates and commodities.
     - Stable Value Guarantees written on $35.7bil pension assets and $4bil of BOLI
     - Derivative counterparty to Municipalities in creating tax-exempt 2a7 paper
     - GIC provider to Municipalities and Tax-Exempt entities (unwinding)
     - Structured Note issuer – roughly $25bil – distributed both wholesale and retail
   - **FP has non-trivial relationships to the parent company and other AIG entities**
     - Large Intercompany Payable - $56bil
       - FP payables to Other AIG Operating Units estimated $1.85bil
         - No collateral arrangements.
         - Sample: ILFC $695mil, MIP $441mil, SunAmericas $240mil, Amer Gen $225mil.
     - Banque AIG – French regulated banking vehicle and key intermediary to clients on derivative trades (eg. Reg arb trades); Exposures back-to-back with FP – collateralized

   - **=> FP failure will transmit losses to parent AIG and other subsidiaries**
   - **Mitigation strategy is to collateralize FP payables to Other AIG Operating Units (does not address exposures to parent)**

2. **FP has Substantial Systemic Relationships with Financial Institutions:**
   - Activities – Derivative counterparty and provider of credit protection.
   - Regulatory Capital Trades provide roughly $11bil of capital relief to European banks
     - Protection written on $240bil of European Mortgages and Corporate Debt
       - Mitigation Strategy – European central banks could recapitalize the banks for the capital relief provided by these trades given the uncertainty of AIG's ability to perform on the contracts
   - Derivative payables to Financial Institutions
     - $9.27bil without collateral
     - $3.59bil after collateral
   - $4.6bil reference notional in CPPI notes and CPPI Gap Risk Insurance on hedge funds and credit portfolios
   - $4bil Stable Value Guarantee on BOLI
   - $34bil FP losses on CDS on subprime CDO – counterparty risk to FP mitigated by collateral posted
   - FP's current derivative market access limited to CS, DB, BofA and RBS

3. **SPVs and Funds:**
   - Activities – Derivative counterparty for hedging
   - Derivative payables to Structured Vehicles and Funds
     - $2.14bil without collateral and $2.09bil after collateral
     - **FP failure may lead to further unwinding of SPVs and sale of assets**
   - Significant replacement risk given stress in structured finance market
   - FP unrealized gains subject to subordination given rating downgrades

4. **Corporates** -
   - Activities – Derivative counterparty and investor in structured notes.
   - Derivative Payables to Corporates:
     - $3.04bil without collateral
     - **$2.52bil after collateral**
   - Sample Corporate Counterparty Exposures due from FP:
     - HP $125mil, EDF $107mil, AXA $113mil, EADS $97mil, GE $75mil, Canada Life $75mil, Daimler $74mil, , Dassault S192mil.

5. Retail and High Net Worth Investors:

- Activities – Investors in Structured Notes and ETFs
    - Distributed through Financial Institutions to global investor community.
    - Wide range of structured returns – usually issued principal protected.
    - Notes issued to all investors (including corporates) roughly $19bil
- $2bil Commodity ETFs distributed to institutional and individual investors

6. Central Banks, Municipalities and Supranationals:

- Activities –
    - Gold leasing from Central Banks
    - GIC Issuer to Municipalities and Tax-Exempt entities
    - Swap counterparty to Municipalities to create tax-exempt 2a7 paper
- **FP failure potentially impairs revenue sources and disrupts financing arrangements for Municipalities and Tax-Exempt entities**
    - Derivative payables due from FP $1.20bil without collateral; $1.19bil with collateral
- Sample Exposures
    - Gold lease in executed on a collateralized and uncollateralized basis
        - FP derivative payables: Belgium $154mil, Swiss $88mil, Austria $86mil.
    - Swap counterparty in Municipal market - $2.6bil notional
        - FP derivative receivables of $335mil (with 23 counterparties)
    - GICs largely repaid or collateralized in last month. $2 bil uncollateralized exposure.

7. Pension Plans:

- Activities - Stable Value Guarantee (SVG) Provider and Hedge Counterparty
- Exposure: SVG wrap on 186 plans with total market value of $35.7bil.
    - Currently FP owes plans on withdrawal – estimated $1.6bil (=SVG less Market Value)
    - **FP failure potentially eliminates $1.6bil in pension wealth**
    - **Risk mitigation potentially obtained via contract assignment**
  - Provide 40 year equity protection to two Austrian pension plans.
    - FP derivative receivable of $100mil; active assignment discussions underway

DRAFT 10/30/2008

AIG and Systemic Risk

On September 16, 2008, the Board of Governors (Board), with the full support of the Secretary of the Treasury, authorized the Federal Reserve Bank of New York (FRBNY), pursuant to section 13(3) of the Federal Reserve Act, to establish a revolving credit facility for AIG under which FRBNY may lend up to an aggregate amount of $85 billion outstanding at any time. At the time the Board acted, the financial and credit markets were experiencing severe stress. This severe stress can be traced back to, among other things, the sharp and broad-based decline in home prices. That decline was the primary factor behind a substantial rise in mortgage delinquencies and defaults, especially on subprime mortgages, and the resul theting substantial drop in values of mortgages as well as mortgage-backed securities and other instruments based on such assets. As a result of these and other factors, short-term funding markets had come under severe stress during the months prior to September 2008, with very high spreads between lending rates and the target federal funds rate and very illiquid trading conditions in term money markets. Those stresses intensified in late August and early September 2008, and these developments had led to a considerable impairment of a broad range of other financial markets.

These events placed significant liquidity pressures on AIG in the period leading up to September 16, 2008, as declines in the prices of mortgage-related assets required AIG to post additional collateral in connection with its CDO and other mortgage-related derivative exposures and as AIG experienced difficulty in raising additional funding in the markets. Given AIG's inability to obtain adequate credit accommodations from banking institutions or in the market, a downgrade of AIG's credit rating, which was then under review by the major credit rating agencies, threatened to prompt a default by the firm, partly by increasing the collateral calls on the institution.

Many of the same factors that created substantial stress for AIG also contributed to the failure of Lehman Brothers Holdings, Inc. on September 15, 2008. The markets, which were already fragile, were absorbing and adjusting to the failure of Lehman Brothers as these stresses bore down on AIG.

Under these circumstances, the potential failure of AIG posed significant systemic risks. A default by AIG on its commercial paper would likely have caused a number of money market mutual funds to "break the buck," potentially triggering runs on those and other money funds. Such a development could have significantly disrupted the market for commercial paper, undermining the ability of major financial and nonfinancial firms to obtain funding. The difficulties also could have spread to other important money markets, which were already under considerable stress. A default by AIG would have imposed a significant burden on its securities lending counterparties, who would have had to either fund or liquidate the securities they had borrowed from AIG in exchange for cash collateral. Large global banks had significant exposure to AIG on various credit facilities. In addition, many banks have purchased credit protection from AIG on CDS contracts that AIG had written to protect the banks against losses on super-senior asset-backed security (ABS) CDOs. While AIG had posted collateral to cover most of its counterparties' exposures on these CDS contracts, some uncollateralized exposure remained and a failure of AIG would have left the banks bearing the risk of losses if the value of the ABS CDOs declined further. Moreover, a failure of AIG would cause the closeout of derivatives contracts in which it is a counterparty, and many firms would have found the contracts difficult to replace.

More broadly, the disorderly failure of AIG would have undermined business and household confidence and increased investor risk aversion. These effects would have contributed to substantially higher borrowing costs, reduced wealth, and materially weaker economic performance.

In light of these and all other facts, the Board determined that, under the circumstances at the time, a disorderly failure of AIG could add to already significant levels of financial market fragility and lead to, among other things, substantially higher borrowing costs, reduced household wealth, and materially weaker economic performance. The authorized credit facility is intended to assist AIG in meeting its obligations as they come due and facilitate a process under which AIG will sell certain of its businesses in an orderly manner, with the least possible disruption to the overall economy.

DATE: November 6, 2008

TO: Board of Governors

FROM: Staff[1]

SUBJECT: Proposed steps to stabilize American International Group, Inc.

ACTION REQUESTED AND SUMMARY: Staff proposes that the Board authorize the Federal Reserve Bank of New York ("FRBNY") to take several actions to prevent the imminent downgrade of the credit rating of American International Group, Inc. ("AIG"), help stabilize the company and its subsidiaries, mitigate the risks to the financial system that might otherwise occur from a downgrade of AIG, and protect the interests of the Federal Reserve, the Treasury Department ("Treasury") and taxpayers. These actions would be taken in conjunction with the purchase by the Treasury of $40 billion in newly issued Senior Preferred Stock from AIG under the Troubled Asset Relief Program established by the Emergency Economic Stabilization Act of 2008 ("EESA").[2]

The proposal is substantially as discussed with Board members in briefings over the past week. Specifically, it is proposed that the Board authorize FRBNY to take the following actions to complement Treasury's investment—

1. Restructure the current revolving credit facility authorized by the Board in September 2008 (the "September Facility") by (i) reducing

[1] Messrs. Alvarez, Ashton and Fallon and Ms. Allison (Legal Division); Messrs. Madigan and Clouse (Monetary Affairs); Ms. Bailey and Mr. Greenlee (Division of Banking Supervision and Regulation); and Mr. Gibson (Division of Research and Statistics).

[2] The current draft term sheet for Treasury's proposed $40 billion preferred stock investment is attached as Appendix A. This investment would be in addition to the preferred stock (which is convertible into 79.9 percent of AIG's common shares) that will be issued to a trust for Treasury's benefit as a result of the Federal Reserve's $85 billion loan to AIG.

its maximum amount to $60 billion from $85 billion, (ii) extending the maturity of the facility from two to five years, (iii) reducing the rate payable on drawn amounts from LIBOR plus 850 basis points to LIBOR plus 300 basis points, and (iv) reducing the fee payable on undrawn but available amounts from 850 basis points to 75 basis points;

2. Extend up to $22.5 billion in secured, non-recourse credit under section 13(3) to a new limited liability company ("Maiden Lane II") for the purpose of partially funding the acquisition by Maiden Lane II from AIG of approximately $23.5 billion (market value) in residential mortgage-backed securities ("RMBS") purchased by AIG with the cash collateral received through the securities lending operations of AIG's regulated insurance subsidiaries. This new facility would eliminate the need for the $37.8 billion securities borrowing facility authorized by the Board for AIG on October 6, 2008 (the "Securities Borrowing Facility") and this facility would be wound down and terminated; and

3. Extend up to $30 billion in secured, non-recourse credit under section 13(3) to a separate, newly formed limited liability company ("Maiden Lane III") for the purpose of partially funding the acquisition by Maiden Lane III from the current counterparties of AIG's Financial Products business unit ("AIGFP") of up to $35 billion (market value) in multi-sector collateralized debt obligations ("CDOs") currently protected by credit default swaps ("CDS") written by AIGFP.

It is anticipated that these actions, if approved, and Treasury's investment would be publicly announced before the U.S. markets open on Monday, November 10, 2008, contemporaneously with AIG's release of its earnings for the third quarter of 2008.

The loans to Maiden Lane II and III would remove from AIG's balance sheet certain assets and exposures that have caused substantial liquidity drains on the company and generated significant losses that have eroded AIG's capital base. These special purpose vehicles, like the similar

Maiden Lane structure used to facilitate the acquisition of Bear Stearns & Companies, Inc., likely would be consolidated on the balance sheet of FRBNY, and the assets so consolidated would be subject to certain mark-to-market volatility. Importantly, AIG would retain a first loss position in both Maiden Lane II and III, and the FRBNY would have a first lien on all of the assets of these entities to secure its senior loans to the entities. In addition, based on estimates prepared by BlackRock, which is serving as financial advisor to the Federal Reserve, it is expected that the assets of each entity will provide sufficient cash flows to repay FRBNY in full over time even under very stressed scenarios, because the intrinsic values of these assets are estimated by BlackRock to be greater than their current market values.

Because the extension of credit to Maiden Lane II would eliminate the need for the $37.8 Securities Borrowing Facility, the proposed actions described above would reduce the aggregate amount of Federal Reserve credit targeted to assist AIG from a current maximum of $122.8 billion to a maximum of $112.5 billion.[3]

BACKGROUND:

During the past few weeks, the major credit rating agencies (S&P, Moody's, Fitch and A.M. Best) have conducted a review of the credit ratings assigned to AIG's senior unsecured debt and insurance company

[3] Certain eligible subsidiaries of AIG also have sold highly rated commercial paper to the Commercial Paper Funding Facility ("CPFF") and this lending is expected to continue under the CPFF so long as the paper of the subsidiaries continues to meet the eligibility requirements of the facility. AIG has reported that the maximum aggregate amount of commercial paper that its subsidiaries may sell to the CPFF under the terms of the program is approximately $20.9 billion. AIG also has stated that the proceeds received through the sale of commercial paper to the CPFF will be used to refinance AIG's outstanding commercial paper as it matures, meet other working capital needs, and make voluntary prepayments on the September Facility.

subsidiaries.[4] During this review, the rating agencies expressed significant concerns with several aspects of AIG's capital structure, financial exposures and operations. In particular, the agencies have indicated that—

- The firm's current leverage is significantly higher than that generally considered acceptable by the agencies to maintain an A or better debt rating;[5]

- The size of the September Facility creates significant structural subordination of AIG's senior, unsecured debt;

- The current interest rates payable on the September Facility may be unsustainable by the company and significantly weaken the company's interest coverage ratio, which is a key metric used by the rating agencies;

- The company will have difficulty in obtaining sufficient value from its planned divestitures to repay the September Facility in full by September 2010 (the current maturity date of this facility) because of the ongoing strains in the financial markets and the recent declines in the share prices of other large insurance firms, who are the natural buyers for most of AIG's principal subsidiaries; and

- The company remains subject to further liquidity and capital depletion from the CDS exposures held by AIGFP and the potential for further write-downs on the portfolio of RMBS acquired with the proceeds of the securities lending program of AIG's regulated insurance subsidiaries.

In addition, AIG recently disclosed to the credit rating agencies the firm's earnings for the quarter ending September 30, 2008. AIG currently expects

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[4] Currently, AIG's senior debt is rated A- by S&P, A3 by Moody's, and A by Fitch. A.M Best has assigned AIG a financial strength rating of A.

[5] For property and casualty/life insurance firms, the rating agencies' guidelines generally permit an A rated firm to have an adjusted leverage ratio (excluding AOCI) of up to 30 to 40 percent (Moody's) or 25 to 35 percent (S&P). AIG's adjusted leverage ratios under Moody's and S&P's guidelines were 58 percent and 54 percent, respectively, as of September 30, 2008.

to announce on Monday, November 10, 2008, losses of approximately $23 billion for the third quarter, an amount that is significantly above analyst loss estimates for the company.

These and other factors likely would cause the credit rating agencies to downgrade the senior unsecured debt of AIG to BBB or below shortly after AIG's earnings announcement. A downgrade of AIG's senior unsecured debt would pose significant new liquidity problems for AIG and likely would adversely impact the ratings, value and operations of the company's principal insurance subsidiaries.[6] For example, it is estimated that a downgrade to BBB would require an additional $42 billion in liquidity to meet collateral calls and termination events on the exposures held by AIGFP alone. The liquidity pressures resulting from a downgrade could well lead to the insolvency and bankruptcy of AIG. Appendix B provides additional information concerning the potential consequences of an AIG bankruptcy on the financial markets. A bankruptcy by AIG also likely would significantly reduce the value of AIG's assets, including the stock of its regulated insurance subsidiaries, which currently serve as collateral for the September Facility.

DISCUSSION OF PROPOSED ACTIONS:

Staff proposes that the Board authorize several actions in conjunction with the Treasury to help (i) stabilize AIG and its subsidiaries, (ii) mitigate the risks to the financial system that might otherwise occur from such a downgrade, and (iii) protect the interests of the Federal Reserve, the Treasury and taxpayers. These actions would preserve the value of the

[6] The rating agencies have policies that typically limit the extent to which a subsidiary's rating may differ from the rating of its parent.

company's assets and subsidiaries and provide the company additional time to realize such value through the orderly sale of assets.

Importantly, S&P, Moody's and Fitch each have indicated that it will retain its current rating on AIG's senior unsecured debt, and A.M. Best will retain its current financial strength rating for AIG, if the complete package of proposals is authorized and executed. S&P and Moody's have indicated that they will keep AIG's ratings on a short-term "negative watch," and will be looking for the company to make progress in the short-term on asset sales and the wind down of AIGFP's general businesses, as well as in retaining insurance business at its regulated subsidiaries. Fitch has indicated that it will adopt a "stable outlook" for the company. Finally, A.M. Best has indicated that it will move AIG from its equivalent of "negative watch" to "negative outlook."

The proposed actions require approval under section 13(3) of the Federal Reserve Act, which generally requires the affirmative vote of at least five Board members. The Board may authorize a discount[7] to an individual, partnership or corporation under section 13(3) only if (i) the Board finds that "unusual and exigent circumstances" exist; (iii) the lending Reserve Bank obtains evidence that the borrower is unable to secure adequate credit accommodations from other banking institutions; and (iii) the notes are indorsed or otherwise secured to the satisfaction of the Reserve Bank.

[7] The Board has long held that a "discount" of a note under section 13(3) includes a broad range of transactions, including a simple advance to the counterparty on a note newly issued or made by the counterparty and a purchase of one or more third-party notes held by the counterparty. Moreover, even if the facilities provided to Maiden Lane II and III were characterized as an acquisition by FRBNY of the assets of these vehicles, the loans would still be a "discount" of notes of an individual, partnership or corporation permitted under section 13(3) because the assets of these limited liability companies will consist exclusively of third-party secured notes (RMBS and CDOs) that are eligible for discount under section 13(3).

As discussed in previous memoranda, the Board has substantial flexibility in assessing whether "unusual and exigent circumstances" exist. In authorizing the $85 billion September Facility, the Board found that the disorderly potential failure of AIG posed significant systemic consequences in light of fragile market conditions. As explained in Appendix B, the systemic consequences of an AIG bankruptcy have decreased somewhat since September, but still remain significant. Moreover, available evidence indicates that AIG remains unable to secure adequate credit accommodations from other banking institutions and that AIG and other entities, including the proposed Maiden Lane II and III special purpose vehicles, are unable to secure adequate credit accommodations from other banking institutions to finance the types of RMBS and multi-sector CDOs that are the subject of the proposed Maiden Lane facilities.

The proposed restructuring would improve the likelihood that the Federal Reserve will be fully secured and repaid on the September Facility. In addition, FRBNY's new advances to Maiden Lane II and III would be secured by the assets of these entities (which would exceed the amount of FRBNY's advances) and would be protected by a first loss position of AIG that is estimated to fully protect repayment of the FRBNY's senior note over time even under very stressed environments. For these reasons, the proposed Board actions are legally permissible under section 13(3) of the Federal Reserve Act.

A. Restructuring of the $85 Billion September Facility

Currently, all advances made under the September Facility, including accrued and unpaid interest and fees, must be repaid in full by AIG no later than September 22, 2010. In addition, advances under the facility bear interest at a rate equal to 3-month LIBOR plus 850 basis points, payable quarterly. AIG also is obligated to pay an ongoing commitment fee each quarter equal to 850 basis points of the average undrawn amount available under the September Facility during the preceding quarter. Interest and the initial and ongoing commitment fees generally are payable through an increase in the outstanding balance of the Credit Facility, with interest thereafter accruing on such balances at the rate of 3-month LIBOR plus 850 basis points. As of November 5, 2008, AIG had approximately $61 billion in advances and fees outstanding under the September Facility.

As noted above, Treasury proposes to acquire $40 billion in newly issued Senior Preferred Stock of AIG. In connection with Treasury's investment, the terms of the September Facility would be modified to—

- Extend the maturity of the loan to five years (i.e., until September 22, 2013);
- Reduce the maximum amount available under the facility from $85 billion to $60 billion upon the acquisition of the Senior Preferred Stock by Treasury;
- Reduce the interest rate payable on outstanding advances to 3-month LIBOR plus 300 basis points; and
- Reduce the ongoing commitment fee on undrawn amounts to 75 basis points.

These modifications will help address the leverage and interest coverage ratio concerns of the credit rating agencies and are more consistent with the stabilized condition and prospects of the company following completion of the proposed package of actions. In addition, these modifications, including in particular the term extension, should improve the likelihood that AIG will be able to repay advances under the facility by providing AIG additional time to execute its large and global divesture program, which is the primary source of funding for repayment of the facility.[8]

Importantly, other material terms of the September Facility would remain unchanged. For example, the facility would still be secured by AIG's pledge or commitment to pledge substantially all of its assets and the assets of its primary non-regulated subsidiaries, including all of AIG's ownership interest in its regulated U.S. subsidiaries and 66 percent of AIG's ownership interest in its regulated foreign subsidiaries.[9] In addition, AIG's obligations under the September Facility would continue to be guaranteed by each of the company's domestic, non-regulated subsidiaries that have more than $50 million in assets. Moreover, the amended Credit Agreement would continue to include provisions designed to ensure that the proceeds of any asset sales to be conducted by AIG are used to permanently repay any outstanding balances under the September Facility.[10]

B. Maiden Lane II Loan

Certain of AIG's regulated insurance subsidiaries conduct a securities lending program under which the subsidiaries lend out investment grade securities in exchange for cash collateral. AIG used the cash collateral obtained through these securities lending transactions to purchase approximately $48.9 billion par value ($31.2 market value) of RMBS and commercial mortgage-backed securities ("CMBS"). AIG has experienced

[8] The Credit Agreement also would be modified to allow AIG to pay dividends on the Preferred Stock acquired by Treasury.

[9] Due to certain restrictions in AIG's certificate of incorporation, certain assets that AIG has agreed to pledge to secure the facility will not be formally pledged until AIG receives shareholder approval at an upcoming meeting to amend these restrictions in its charter. AIG would incur adverse tax consequences if it were to pledge more than 66 percent of its ownership interest in its regulated foreign subsidiaries.

[10] The terms of the new Treasury Preferred Stock also would prohibit any redemptions of such stock by AIG until the modified September Facility is fully paid.

significant liquidity pressures as its securities lending counterparties have pulled away from the company. On October 6, 2008, the Board authorized the creation of the $37.8 billion Securities Borrowing Facility for AIG to address the immediate liquidity needs caused by the ongoing withdrawal of AIG's securities lending counterparties.[11]

AIG, however, remains exposed to further declines in the value of the securities in the reinvestment portfolio, particularly the RMBS securities (approximately $39.6 billion par value) that primarily compose this portfolio. This exposure puts ongoing stress on the liquidity and capital of AIG and weakens the company. It also is of concern to the rating agencies. AIG already has experienced approximately $16.1 billion in mark-to-market losses on these RMBS (as of September 30, 2008) and the market for these securities currently is illiquid. To address these concerns, it is proposed that AIG sell all of the RMBS in the reinvestment portfolio to a new limited liability company, Maiden Lane II, that would be established solely for the purpose of holding these assets.

Under the proposal, AIG would provide $1 billion in equity to Maiden Lane II in the form of a subordinated loan, and FRBNY would extend up to $22.5 billion in senior credit on a non-recourse basis to the limited liability company under section 13(3). The senior loan from FRBNY would have a maturity of six years, subject to extension by the Reserve Bank. The aggregate proceeds of the subordinated and senior notes would be used to purchase the RMBS portfolio from AIG at the market value of the RMBS as of October 31, 2008, as determined in consultation with BlackRock, which

[11] This facility essentially permitted FRBNY to replace all of AIG's existing securities lending counterparties if necessary. As of November 5, 2008, approximately $20 billion was outstanding under this facility.

is advising the Federal Reserve. The market value of the RMBS was $23.5 billion as of September 30, 2008, based on AIG's marks. It is expected that the October 31 marks will be lower, which will reduce the size of the senior loan from FRBNY on a dollar-for-dollar basis. AIG's subordinated equity position ($1 billion) in Maiden Lane II was sized to fully protect FRBNY's senior note while also limiting the immediate and potential future cash drains on AIG from its retained position in the RMBS portfolio.

In addition to reducing the strain on AIG from its RMBS exposures, the Maiden Lane II facility would eliminate the need for the $37.8 billion Securities Borrowing Facility. Accordingly, this existing facility would be wound down and terminated, primarily through the use of the proceeds from the Maiden Lane II facility to close out securities borrowing transactions as they come due.[12]

The senior financing provided by the FRBNY would earn interest at a rate of 1-month LIBOR plus 100 basis points and all incoming cash flows would be applied to the senior debt until principal and interest on the note is fully paid (expected to occur between 2014 and 2019 under the scenarios modeled by BlackRock). AIG's subordinated first loss position in Maiden Lane II would accrue interest at a rate of 1-month LIBOR plus 300 basis points, but AIG will receive no cash payments until the principal and interest on the senior debt is fully repaid. After both the senior debt position and AIG's subordinated position are fully repaid, any residual returns will be

[12] To fully wind down the Securities Borrowing Facility, AIG must receive approval from the relevant insurance authorities to have the insurance subsidiaries participating in the securities lending program purchase the approximately $9.3 billion par value ($6 billion market value) of CMBS remaining in the reinvestment portfolio. AIG expects to be able to receive such approvals promptly once the package of proposed actions is announced.

apportioned 5/6th to FRBNY and 1/6th to AIG. Although the rating agencies have expressed concern about AIG's continuing downside exposure to the RMBS, the rating agencies also have indicated that they believe it is important for the company retain some upside in the portfolio, which is why AIG would share some portion of the residual cash flows.

It is expected that Maiden Lane II would be consolidated on the balance sheet of FRBNY. A financial advisor would be hired by FRBNY to manage Maiden Lane II's assets with a view toward maximizing repayment of its obligations with minimum disruption to the financial markets.

The FRBNY loan would be secured by the entire portfolio of RMBS acquired by Maiden Lane II (including the proceeds of any sale or repayment at maturity of such assets) and these RMBS are in turn secured by interests in residential mortgages.[13] The RMBS are backed primarily by subprime and Alt-A residential mortgages and are primarily rated AAA (47.1 percent), although approximately 15 percent of the portfolio is rated lower than BBB or not rated.[14] Because the estimated intrinsic values of the RMBS are greater than current market values, BlackRock projects that, even under very stressed scenarios, the FRBNY senior financing would be repaid over time. However, because the market values of these assets are volatile

[13] Section 110 of the Emergency Economic Stabilization Act requires that the Board implement a plan to maximize assistance to homeowners and reduce foreclosures with respect to residential mortgages and RMBS owned or controlled by a Reserve Bank. These provisions, however, do not apply to mortgages or RMBS (i) held as collateral for a discount window loan that is not in default, or (ii) acquired in open market operations. Accordingly, these provisions would not apply to the residential mortgage-related assets to be acquired by Maiden Lane II or III unless and until the FRBNY's loans to such entities were in default. Federal Reserve staff currently are drafting foreclosure mitigation policies that would meet the requirements of section 110 if triggered.

[14] These data are based on the lowest rating given by any of the three major rating agencies to the assets.

and would be reflected on the balance sheet of FRBNY, it is estimated that the transaction would result in approximately $1.5 to $2.6 billion in quarterly mark-to-market volatility on FRBNY's balance sheet at least in the short run.

C. Maiden Lane III Loan

One of the greatest strains on AIG arises from the derivative exposures of AIGFP and, in particular, the exposures arising from approximately 140 CDS contracts written by AIGFP on mortgage-related multi-sector CDOs with about 20 financial institution counterparties.[15] Under the CDS, AIG has provided counterparties with credit protection on specific CDOs (the "reference securities"). In particular, AIG has agreed to purchase the reference security at par in the event of a credit event (e.g., a downgrade or default) during the term of the CDS. In return, AIG receives an upfront or periodic fee from the counterparty.

The total notional amount of the multi-sector CDOs on which AIGFP had written credit protection is approximately $65 billion. As the mark-to-market value of the CDOs has declined, AIG has been required to post collateral with the counterparties to secure its payment in the event of a credit event and has incurred fair value losses on the CDS derivatives based on such assets. As of October 24, AIG had posted approximately $30.3 billion in collateral with its multi-sector CDO counterparties. Further declines in the market value of the reference CDOs would require AIG to provide additional collateral to the counterparties, creating a significant

[15] The data in this section excludes one relatively small ($1.8 billion) CDS exposure on a synthetic multi-sector CDO that would be excluded from the Maiden Lane III facility for operational and legal reasons.

potential liquidity drain on the company and additional fair value losses for the company.

To address these concerns, a proposed credit facility has been developed to substantially reduce AIG's exposure to the multi-sector CDOs, which has been the single greatest source of losses for AIGFP. In order to implement this facility, AIG's multi-sector CDO counterparties must first agree to "tear up" their CDS contract with AIGFP. In return for doing so, AIG would agree to purchase from the counterparty the CDO reference asset underlying the CDS at par, less a concession amount to be negotiated with the counterparty.[16] The CDOs acquired by AIGFP would then be sold to Maiden Lane III, a separate limited liability company established for the sole purpose of holding these CDOs.

The funding for AIGFP's purchases of the CDOs from the counterparties would come from two sources. First, the counterparties would retain the cash collateral that AIGFP had already posted with respect to the CDS (approximately $30.3 billion). If necessary, AIGFP would provide additional collateral (that also would be retained by the counterparty) to bring the collateral amount in line with a mutually agreed market value of the CDOs on or near the tear up date. The amount of additional collateral that AIGFP will need to post through this process currently is estimated to be in the range of $4 billion to $6 billion.

[16] Certain counterparties may not own the CDOs underlying the CDS, in which case the counterparty would have to obtain the CDO reference asset (or a CDO with substantially similar characteristics) to engage in the tear up process and receive funding from the Maiden Lane III facility.

The remaining cash needed to fund the purchase[17] of the CDOs by AIGFP would come from Maiden Lane III. AIG would provide $5 billion in equity to Maiden Lane III in the form of a subordinated loan. The FRBNY would make a non-recourse senior loan to Maiden Lane III of up to $30 billion under section 13(3).[18] AIGFP would immediately transfer the CDOs purchased to Maiden Lane III, effectively completing the purchase of the CDOs by Maiden Lane III at their then current market value. The CDOs would then collateralize the loan from FRBNY. These transactions may take place at different times with different counterparties, with the amount of the senior note increasing over time as the transactions with additional counterparties are consummated.

It is expected that Maiden Lane III would be consolidated on the balance sheet of FRBNY. A financial advisor would be hired by FRBNY to manage Maiden Lane III's assets with a view toward maximizing repayment of its obligations with minimum disruption to the financial markets.

Like the proposed Maiden Lane II loan, the interest rate on the FRBNY loan to Maiden Lane III would be 1-month LIBOR plus 100 basis points and the rate on the AIG subordinated loan would be 1-month LIBOR plus 300 basis points. All cash flows from the CDO assets would be applied first to the senior note until principal and interest on the note was paid in full

[17] Remaining amount = $65 billion par value of CDOs less $30.3 billion posted collateral less the additional collateral to be posted by AIGFP less any concession obtained from the counterparty.

[18] The $30 billion is the maximum amount of senior financing that would be provided by FRBNY to Maiden Lane III and would be reduced by the estimated $4 billion to $6 billion of additional collateral that AIGFP will have to post prior to the tear up of the CDS as well as any concessions obtained from the counterparties. In addition, some of AIGFP's counterparties may elect not to participate in the tear up process and others representing smaller exposures may be excluded from the process for technical or operational reasons.

(expected to be between October 2013 and July 2014 under the scenarios modeled by BlackRock), and would then be applied to the junior note until it was repaid in full. Any residual cash flows would be divided between FRBNY (67 percent) and AIGFP (33 percent). The FRBNY's senior loan would have a maturity of six years, subject to extension by the FRBNY.

AIG's equity position in Maiden Lane III ($5 billion) again was sized to fully protect the FRBNY's senior position under a variety of stress scenarios, while limiting the continuing downside exposure of AIG to the multi-sector CDOs, a significant concern of the rating agencies. The residual interest split also was designed to address a concern expressed by the rating agencies—that AIG receive a fair return for the risk taken on its equity contribution and have some opportunity to share in the upside of these currently distressed assets.

The primary assets backing the CDOs are residential mortgages (52 percent subprime and Alt-A U.S. RMBS by dollar amount), with the remaining assets composed of CMBS (18 percent), prime or agency-guaranteed mortgage-backed securities (17 percent), other CDOs (10 percent) and other asset-backed securities (2 percent). Ratings on these assets are distributed from Aaa (36 percent) to below Baa3 (18 percent), with approximately 90 percent of the underlying collateral having been originated between 2004 and 2007.

Cash flow projections prepared by BlackRock indicate that, even in relatively extreme stress scenarios, the FRBNY's senior note is likely to be repaid in full over time. However, because the market values of these assets are volatile and would be reflected on the balance sheet of FRBNY, it is estimated that the transaction would result in approximately $3.2 to

$4.0 billion in quarterly mark-to-market volatility on FRBNY's balance sheet at least in the short run.

Attachments

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APPENDIX A:

TARP Capital Purchase Program

Senior Preferred Stock

Summary of Senior Preferred Terms

Issuer:	American International Group, Inc. ("AIG").
Initial Holder:	United States Department of the Treasury (the "UST").
Size:	$40 Billion aggregate liquidation preference.
Security:	Senior Preferred, liquidation preference $10,000 per share; provided that UST may, upon transfer of the Senior Preferred, require AIG to appoint a depositary to hold the Senior Preferred and issue depositary receipts.
Ranking:	Senior to common stock and pari passu with existing preferred shares other than preferred shares which by their terms rank junior to the Senior Preferred. At the meeting of stockholders called to effect the amendments to AIG's Restated Certificate of Incorporation contemplated by the terms of the convertible preferred stock, AIG shall propose amendment to its Restated Certificate of Incorporation to allow the Senior Preferred to rank senior to the convertible preferred stock.
Term:	Perpetual life.
Dividend:	The Senior Preferred will accrue cumulative dividends at a rate of 9% per annum. Dividends will be payable quarterly in arrears on [ ], [ ], [ ] and [ ] of each year. Dividends will be payable when, as and if declared by the Board of Directors of AIG. Accrued but unpaid dividends shall compound quarterly.
Redemption:	Senior Preferred may be redeemed, in whole or in part, at any time and from time to time, at the option of AIG to the extent the senior secured revolving credit facility governed by the Credit Agreement dated as of September 22, 2008 (the "Credit Agreement") between AIG and the Federal Reserve Bank of New York ("FRBNY") is terminated. All redemptions of the Senior Preferred shall be at 100% of its issue price, plus an amount equal to accrued and unpaid dividends (including, if applicable, dividends on such amount).
Restrictions on Dividends:	Subject to certain exceptions, for as long as any Senior Preferred is outstanding, no dividends may be declared or paid on junior preferred shares, preferred shares ranking pari passu with the Senior Preferred ("Parity Stock"), or common shares (other than (i) in the case of pari passu preferred shares, dividends on a pro

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rata basis with the Senior Preferred and (ii) in the case of junior preferred shares, dividends payable solely in common shares), nor may AIG repurchase or redeem any junior preferred shares, preferred shares ranking pari passu with the Senior Preferred or common shares, unless all accrued and unpaid dividends for all past dividend periods on the Senior Preferred are fully paid or declared and a sum sufficient for the payment thereof set apart.

Common dividends: The UST's consent shall be required for any increase in common dividends per share until the fifth anniversary of the date of this investment unless prior to such fifth anniversary the Senior Preferred is redeemed in whole or the UST has transferred all of the Senior Preferred to third parties.

Repurchases: The UST's consent shall be required for repurchases of any common shares, other capital stock, trust preferred securities or other equity securities (other than (i) repurchases of the Senior Preferred, (ii) repurchases of junior preferred shares or common shares ("Junior Stock") in connection with the administration of any employee benefit plan in the ordinary course of business and consistent with past practice (including purchases to offset share dilution pursuant to a publicly announced repurchase plan), (iii) any redemption or repurchase of rights pursuant to any stockholders' rights plan and (iv) the exchange or conversion of Junior Stock for or into other Junior Stock or of Parity Stock or trust preferred securities for or into other Parity Stock (with the same or lesser aggregate liquidation amount) or Junior Stock, in each case, solely to the extent required pursuant to binding contractual agreements entered into prior to the signing date of UST's agreement to purchase the Senior Preferred or any subsequent agreement for the accelerated exercise, settlement or exchange thereof for common stock), until the fifth anniversary of the date of this investment unless prior to such fifth anniversary the Senior Preferred is redeemed in whole or the UST has transferred all of the Senior Preferred to third parties.

Voting rights: The Senior Preferred shall be non-voting, other than class voting rights on (i) any authorization or issuance of shares ranking senior or pari passu to the Senior Preferred, (ii) any amendment that adversely affects the rights of Senior Preferred, or (iii) any merger, exchange or similar transaction unless the Senior Preferred remains outstanding or is converted into or exchanged for preference securities of the surviving or resulting entity or its ultimate parent and the Senior Preferred or such preference shares have such rights, preferences, privileges and voting powers, and limitations and restrictions thereof, taken as a whole, as are not materially less favorable to the holders thereof than those of the Senior Preferred immediately prior to such transaction, taken as a whole.

If dividends on the Senior Preferred are not paid in full for four dividend periods, whether or not consecutive, the Senior Preferred will have the right to elect the greater of 2 directors and a number of directors (rounded upward) equal to 20% of the total number of directors after giving effect to such election. The right to elect directors will end when full dividends have been paid for

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all past dividend periods.

Transferability:	The Senior Preferred will not be subject to any contractual restrictions on transfer other than such as are necessary to insure compliance with U.S. federal and state securities laws. AIG will file a registration statement (which may be a shelf registration statement) covering the Senior Preferred as promptly as practicable, but in any event within 15 days, after notification by UST and, if necessary, shall take all action required to cause such registration statement to be declared effective as soon as possible. During any period that an effective registration statement is not available for the resale by AIG of the Senior Preferred, AIG will also grant to the UST piggyback registration rights for the Senior Preferred and will take such other steps as may be reasonably requested to facilitate the transfer of the Senior Preferred including, if requested by the UST, using reasonable best efforts to list the Senior Preferred on a national securities exchange. If requested by the UST, AIG will appoint a depositary to hold the Senior Preferred and issue depositary receipts.
Claim in Bankruptcy:	Equity claim with liquidation preference to common equity claim.
Acceleration Rights:	None
Use of Proceeds:	To repay the senior secured revolving credit facility governed by the Credit Agreement.
Tax Treatment:	Dividends on the Senior Preferred are non tax-deductible to AIG.
Restrictions on Expenses:	AIG shall continue to maintain and implement its comprehensive written policy on corporate expenses and distribute such policy to all AIG employees. Such policy, as may be amended from time to time, shall remain in effect at least until such time as any of the shares of the Senior Preferred are owned by UST. Any material amendments to such policy shall require the prior written consent of UST until such time as UST no longer owns any shares of Senior Preferred, and any material deviations from such policy, whether in contravention thereof or pursuant to waivers provided for thereunder, shall promptly be reported to UST. Such policy shall, at a minimum: (i) require compliance with all applicable law; (ii) apply to AIG and all of its subsidiaries; (iii) govern (a) the hosting, sponsorship or other payment for conferences and events, (b) the use of corporate aircraft, (c) travel accommodations and expenditures, (d) consulting arrangements with outside service providers, (e) any new lease or acquisition of real estate, (f) expenses relating to office or facility renovations or relocations and (g) expenses relating to entertainment or holiday parties; and (iv) provide for (a) internal reporting and oversight and (b) mechanisms for addressing non-compliance with the policy.
Restrictions on Lobbying:	AIG shall continue to maintain and implement its comprehensive

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written policy on lobbying, governmental ethics and political activity and distribute such policy to all AIG employees and lobbying firms involved in any such activity. Such policy, as may be amended from time to time, shall remain in effect at least until such time as any of the shares of the Senior Preferred are owned by UST. Any material amendments to such policy shall require the prior written consent of UST until such time as UST no longer owns any shares of Senior Preferred, and any material deviations from such policy, whether in contravention thereof or pursuant to waivers provided for thereunder, shall promptly be reported to UST. Such policy shall, at a minimum: (i) require compliance with all applicable law; (ii) apply to AIG and all of its subsidiaries and affiliated foundations; (iii) govern (a) the provision of items of value to any government officials, (b) lobbying and (c) political activities and contributions; and (iv) provide for (a) internal reporting and oversight and (b) mechanisms for addressing non-compliance with the policy.

Reporting: Except as otherwise agreed [and subject to UST entering into a customary confidentiality agreement], AIG shall provide UST (i) the information required to be provided by AIG to the FRBNY pursuant to Section 5.04 of the Credit Agreement and (ii) the notices required by Section 5.05 of the Credit Agreement, in each case within the time periods for delivery thereof specified in the Credit Agreement; provided that as of the time that the senior secured revolving credit facility governed by the Credit Agreement is repaid in full such informational and notice requirements as are provided in Section 5.04 and Section 5.05 of the Credit Agreement shall remain in full force and effect until such time as UST no longer owns any shares of Senior Preferred. In addition, AIG shall promptly provide UST such other information and notices as UST may reasonably request from time to time.

Executive Compensation: [To Be Added – This will cover all of the provisions of TARP plus such additional limitations with respect to severance, bonuses and senior executive compensation for Systemically Significant Financial Institutions as may be reasonably requested by UST within [45] days of the date of this investment.]

Risk Management Committee: AIG shall establish, within [30] days of the issuance of the Senior Preferred, and maintain, at least until UST ceases to own any shares of the Senior Preferred, a risk management committee of the Board of Directors that will seek to identify the major risks involved in AIG's business operations and review the quality of AIG's actions to mitigate and manage those risks.

APPENDIX B:

Systemic risks of AIG[1]

November 3, 2008

Introduction

In this memo, I discuss the possible systemic risks from a failure of AIG. The particular scenario considered is a bankruptcy filing by AIG, Inc., the parent holding company, and AIG Financial Products Corp. (AIGFP), with AIG's insurance subsidiaries entering a rehabilitation process overseen by domestic and foreign regulators. Much of the information used to prepare this memo was provided by management representations at AIG. In many cases, information is incomplete and the memo's conclusions should be viewed as preliminary.

Market confidence

The largest systemic risk at present is the risk to market confidence from a failure of AIG. Market confidence is in a fragile state after the intense financial turmoil of recent weeks. Treasury and the Federal Reserve have taken a range of actions, including the initial decision to lend to AIG. A broadening of government support for financial institutions has appeared to help stop the loss of market confidence in the financial system. A failure of AIG would call into question the ability of that broader government support to be sustained. This risk is impossible to quantify.

Exposures to AIGFP

AIGFP, AIG's capital markets and derivatives subsidiary, contains a number of systemic risks. I describe six of the important risks below. Given the range of risks present within AIGFP, there are undoubtedly some important risks that have been omitted from this list.

1. CDS written on ABS CDOs

AIGFP wrote credit protection on super-senior tranches of ABS CDOs and is exposed to the subprime mortgage-backed securities that the ABS CDOs own. The current notional amount of AIG's positions is $71 billion. AIG has taken $33 billion of writedowns on these positions as of September 30, 2008 and has posted collateral to its counterparties of $33 billion.

If AIG fails, its counterparties would face a loss on whatever uncollateralized exposure exists at that time. Counterparties have marked these positions down by $4 billion since September 30 (for a cumulative mark-to-market of $37 billion) and are

[1] This memo is a staff product and does not represent any formal finding by the Board about systemic risk effects.

currently asking for that amount of additional collateral. AIG is disputing those marks and has not posted the additional collateral. If AIG fails, its counterparties would bear the $4 billion loss.

Many of the counterparties own the underlying CDO securities against which AIG wrote credit protection or have other hedges. They would be left with up to $38 billion of unhedged super-senior ABS CDO risk if AIG failed. Because these positions are extremely sensitive to further house price declines, it would be expensive for AIG's counterparties to replace these positions. This would cause additional losses beyond the $4 billion described above.

At the time of the September 16 loan, the notional value of CDS written on ABS CDOs was $80 billion. AIG had taken $25 billion of writedowns as of June 30 and had posted $16 billion of collateral, leaving AIG's counterparties with an exposure of $9 billion. Systemic risk has fallen since September 16 because AIG has drawn on the Federal Reserve's $85 billion facility to post collateral against this $9 billion.

2. Regulatory capital arbitrage CDS

AIG wrote credit protection on super-senior tranches of corporate loan and prime mortgage exposures held by European banks in order to provide those banks with a regulatory capital reduction under their national implementations of Basel 1 capital standards.[2] AIG's largest counterparties are French, German, Dutch, Danish and Swedish banks. The notional amount outstanding has fallen from $379 billion at year-end 2007 to $240 billion at October 13, 2008. The portfolio is running off quickly because the counterparties have the option to terminate the trades when they go live onto Basel 2. The capital relief for AIG's European bank counterparties is currently estimated at between $2.4 and $11.1 billion, depending on where each bank's transition from Basel 1 to Basel 2 stands.[3] AIG's current mark-to-market loss is only $160 million, reflecting the fact that these trades were structured to transfer no credit risk, merely to provide regulatory capital relief.

If AIG fails, the Basel 1 risk-weighted assets reported by its counterparties would increase, resulting in a regulatory capital hole of up to $11.1 billion. Although the market knows this aggregate amount already from AIG's public disclosures, AIG's failure would reveal to the market which particular banks had shored up their Basel 1 capital ratios in this way.

Compared with the time of the September 16 loan, systemic risk is lower because the notional amount of trades is lower (it was $305 billion on June 30) and because European governments have put measures in place to guarantee bank liabilities and inject capital into banks.

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[2] These trades would not have provided capital relief under the U.S. implementation of Basel 1 capital standards.
[3] To avoid shouting "Fire!" in a crowded theater, we have not approached the European regulators to quantify the capital relief more precisely.

3. Intra-company exposures to AIGFP[4]

AIG's other subsidiaries have material exposures to AIGFP on OTC derivatives. The largest exposures are at finance company affiliates ($920 million) and the funds management affiliate ($441 million). Insurance affiliates are owed approximately $475 million. In addition, these affiliates would have to replace these hedges (primarily interest rate and foreign currency derivatives) at a time when markets are volatile.

A default of AIGFP would have a catastrophic impact on Banque AIG, a French bank that is a wholly-owned subsidiary of AIGFP and through which AIGFP executed many of its OTC derivative trades. For example, Banque AIG is the counterparty to the European banks' regulatory capital trades. All the exposures in Banque AIG's trades are hedged with back-to-back trades with AIGFP.

Systemic risk from these intra-company exposures is high. In particular, the failure of Banque AIG (a regulated bank) could have a more damaging effect on market confidence than the failure of AIGFP (an unregulated derivatives product subsidiary). Through the intra-company exposures, the failure of AIGFP would cause significant loss of value at AIG's other subsidiaries, many of which are expected to be sold to repay the Federal Reserve's loan.

4. Stable value wraps

AIGFP has provided stable value wraps, referred to as Benefit Responsive Options (BROs), for 401k plan participants. AIG guarantees that plan participants can receive book value for qualified withdrawals, although AIG is not required to make any payments until after a fund's assets are depleted through qualified withdrawals. AIG had a notional value of $36 billion of BROs at September 30, 2008 with 175 plan counterparties. The aggregate market-to-book ratio was estimated at 95.5 percent at September 30, leaving AIG with an exposure of $1.6 billion.

Systemic risk of these stable value wraps is high. Although the exposure amount is not large and it is unlikely that AIG will have to make any payments, market confidence would be affected if plan sponsors are forced to notify plan participants that their investments in stable value funds are no longer guaranteed (at the same time that turmoil in credit markets is pushing down the market value of the funds' investments). This risk is falling over time, as plan sponsors replace AIG as the stable value wrap counterparty when contracts are renewed. Deals with aggregate book value of $3.3 billion were terminated before September 30.

5. AIGFP's liabilities

Some of AIGFP's liabilities may pose a systemic risk. These include guaranteed investment contracts (GICs) and debt securities. GICs have been issued to a variety of

[4] This section relies on analysis done by John Kambhu.

counterparties including municipalities. AIGFP has $11.4 billion of GICs outstanding, of which $9.7 billion is collateralized. Much of AIGFP's $35 billion outstanding of debt securities was structured to provide a counterparty with a market risk exposure (to interest rate, equity, commodity, or foreign exchange rate risk). Some was sold to banks and institutional investors who passed the market risk through to individual high net worth investors, and some was sold directly to investors who are exposed to an AIG default.

Systemic risk on GICs has fallen considerably since September 16, when GICs outstanding were $19 billion, of which about $12 billion was uncollateralized. Only $1.7 billion of uncollateralized exposure on GICs remains. Systemic risk on debt securities is still high, as these have a longer maturity and no collateral requirements. If AIG defaults, AIGFP's counterparties on structured notes – banks and institutional investors – would suffer a direct loss of principal and would also be left with an open risk position vis-à-vis their customers to whom they passed through the market risk exposures. While AIG's counterparties have had ample opportunity to hedge their exposure to an AIG default, we do not know who the counterparties are or whether they have hedged.

6. OTC derivatives

Some of AIGFP's OTC derivatives counterparties have uncollateralized exposures that would result in a loss if AIG defaults. The most recent data available on derivatives payables as of September 23 showed the top 50 counterparty exposures summed to $4.5 billion. The largest exposures were to securitization trusts (for interest rate swaps that enable the trust to match the interest rate risk of its assets and liabilities), financial institutions, corporates, and sovereigns.

Systemic risk may be highest for the securitization trusts and financial institutions. Many investors in mortgage-backed securities or asset-backed securities would be surprised to learn that an AIG default could have an impact on their investment, since securitization trusts are designed to be "bankruptcy remote," which could have knock-on effects in broader securitization markets. Lehman Brothers also had OTC derivatives outstanding with a large number of securitization trusts. As a result of Lehman's bankruptcy, many of those transactions have been downgraded by rating agencies, and investors may suffer losses.

Financial institutions that reported a material loss to AIG on OTC derivatives could suffer a loss of market confidence. However, most of AIG's counterparties with large OTC derivatives exposures are European banks whose governments have already put in place extraordinary measures to support their national banking systems.

If AIG fails and its OTC derivatives book is unwound, counterparties would be forced to replace their positions with AIG or retain an unhedged risk position. When Lehman Brothers failed, this was a major concern, but rehedging of Lehman's OTC derivatives did not turn out to have systemic effects. Lehman's OTC derivatives book was ten times larger than AIG's (measured by notional amount) which suggests that this risk may not be large.

However, to the extent that AIG's book of OTC derivatives has a different character than Lehman's, there may be additional systemic risk concerns. Some of AIG's OTC derivatives trades are different because they were done solely to exploit AIG's AAA rating. For example, AIG is an intermediary on a set of 30-year natural gas swaps between Goldman Sachs and the Southern California Public Power Authority (which provides electricity to Los Angeles and other cities in Southern California). Presumably the Power Authority was uncomfortable with Goldman Sachs as counterparty on a 30-year trade and was willing to pay a premium for the comfort of an AAA-rated counterparty. AIG's failure would leave both counterparties with a large open risk position that they would need to rehedge (presumably they could rehedge with each other). In addition, AIGFP also has an exotic derivatives book whose positions could prove difficult for counterparties to replace in current market conditions.

Another systemic risk consideration is the operational burden on OTC derivatives markets of coping with the default of a large counterparty who is also a common reference entity in CDS. The Lehman Brothers default strained the market's operational capacity, but the fear that operational failures would cause systemic risks did not materialize. However, the market may not have had the capacity to simultaneously cope with an AIGFP bankruptcy and a Lehman Brothers bankruptcy. This aspect of systemic risk from AIG has fallen, since more than a month has passed since Lehman's bankruptcy.

Commercial paper

AIG, AIGFP, and two of AIG's finance subsidiaries have $6.9 billion of commercial paper outstanding as of October 22, 2008. Of the $6.9 billion, $4.2 billion is asset-backed commercial paper (ABCP) and the remainder is unsecured. The bankruptcy of Lehman Brothers demonstrated how commercial paper held by money market mutual funds could pose a systemic risk. We do not know who is holding AIG's commercial paper, but presumably this risk is still high.

However, the systemic risk from AIG's commercial paper has diminished since September 16, when AIG had $19.7 billion of CP outstanding. Of the $19.7 billion, $5.1 billion was ABCP. Since then, the Federal Reserve has established three lending facilities (AMLF, CPFF, and MMIFF) to reduce the systemic risk related to commercial paper and money market mutual funds.

Securities lending

AIG still has approximately $20 billion of borrowings from banks and broker-dealers remaining in its securities lending program. If AIG fails, the securities lending counterparties could receive ownership of the securities in lieu of receiving their cash.

These securities are high-grade corporate bonds and agency MBS, so credit losses are not expected, but this could have a material funding impact on those counterparties.

However, the systemic risk impact of the securities lending program is lower now than it was on September 16, when AIG had approximately $69 billion in liabilities and funding markets were under tremendous strain from the Lehman Brothers bankruptcy. The amount outstanding has fallen as counterparties have refused to roll over their securities lending transactions with AIG. A wider array of Federal Reserve lending facilities to support short-term funding markets is now available to help AIG's counterparties deal with the funding impact of an AIG default.

Insurance subsidiaries

AIG's regulated insurance subsidiaries, both domestic and foreign, would be affected by the default of the AIG parent holding company. State regulators have stated that the insurance companies they regulate are capitalized on a stand-alone basis and can maintain claims-paying ability to benefit policyholders. Conseco filed bankruptcy in 2002 due to losses in its consumer finance subsidiary, but its insurance companies continued to operate. If AIG's insurance subsidiaries are unable to continue operating following an AIG default, they could be seized by state regulators and put into rehabilitation.

It is possible that the failure of the AIG parent holding company could lead to additional losses at AIG's insurance subsidiaries. The intra-company exposures discussed above are one possible channel for this to occur. If an insurance company is found to be insolvent, its regulator may choose to liquidate it. In that event, a state guaranty fund will pay claims, up to a cap, and may provide for continuing coverage by transferring the policies to another insurance company.

Whether AIG's insurance subsidiaries are put into rehabilitation or whether they are liquidated, a potential systemic risk exists if the public loses confidence in insurance companies more broadly. For example, life insurance companies are vulnerable to a run by policyholders with cash value policies.

Direct credit exposures to AIG

On September 16, AIG reported that banks had $30 billion in exposure to it on various bank loan facilities and lines of credit, of which about $7 billion was to U.S. institutions. A more recent measure of direct credit exposure is not available.

Alternatives for CDO Book

November 4, 2008

PRELIMINARY DRAFT FOR DISCUSSION PURPOSES

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Overview of Options

We re-considered the options available to the FRB-NY regarding the AIG multi-sector CDO book

We focused on three:

1. *Two-tiered SPV* (currently on the table)
2. *Reverse novation* (FRB-NY steps into the counterparties' shoes)
3. *Straight repo* (simplest, eliminates all swaps - could be a transitional step)

In all options, the counterparties get paid near or at par

Option 3 is the simplest / fastest way to execute - and with counterparties out of the way, it may serve as a way station even if #1 is the ultimate goal

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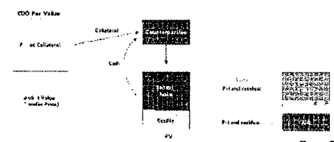
Option 1: Two-Tier Structure

Description: Fund SPV; buy bonds; tear up swaps; 2-tier structure (AIG equity, FRB-NY senior note)

Objective: Caps AIG's liquidity and capital risk; leaves upside for FRB-NY

Evaluation:

- Secure structure for FRB-NY
- AIG loses large portion of upside
- FRB-NY consolidates



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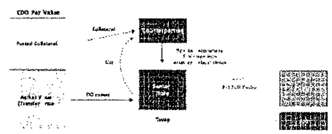
Option 2: Reverse Novation

Description: SPV steps into shoes of counterparties, but with a more lenient CSA based on modeled stress outcomes

Objective: Reduce collateral posting drain, but keep long-term CDO exposure within AIG

Evaluation:

- AIG retains collateral risk (including upside)
- AIG may not need to consolidate (remains a derivative exposure, balance sheet expands as CDS events / funding)
- Fed exposed to risk of AIG default (but transfer price can be adjusted to reduce exposure to Option 1 levels)



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Option 3: Tear Up All Swaps, no SPV

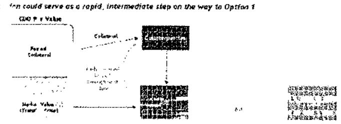
Description: Tear up all swaps at or near par, and FRBNY provides term repo for AIG to fund purchase; AIG posts collateral based on *modeled* extreme stress (not market value)

Objective: reduce liquidity drain on AIG, but keep long-term CDS exposure within AIG (in form of CDOs)

Evaluation (similar to #2, but simpler)

- AIG retains collateral risk
- AIG consolidates
- FRB-NY exposed to AIG counterparty risk (but transfer price can be adjusted)

This c [illegible] could serve as a rapid, intermediate step on the way to Option 1



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FRBNY-TOWNS-R1-102409

Sarah Dahlgren/NY/FRS
11/06/2008 10:02 PM

To: Meg McConnell/NY/FRS
cc:
bcc:
Subject: Fw: DRAFT of AIG Justification Memo

how should we respond?...I haven't been able to get past page 2......any luck on your side?

* * * * * * * * * * * * * *
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----- Forwarded by Sarah Dahlgren/NY/FRS on 11/06/2008 09:41 PM -----

Matthew.Rutherford@do.treas.gov
11/06/2008 03:33 PM

To: Meg.McConnell@ny.frb.org, Sarah.Dahlgren@ny.frb.org
cc:
Subject: DRAFT of AIG Justification Memo

Meg and Sarah:

Attached is a draft of the Treasury AIG justification memo. I have deleted sections 4 through 7 because they are all in flux, but please take a look at what I wrote this past weekend for sections 1 through 3. Most folks here (GC on down) have seen this already and have signed off, so just take a look at the content, particularly in the Fed section. You will see that I used some of the Fed's language in the second section.

Many thanks. Please don't pass this memo along to anyone else.

Matt

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