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************EXCERPTS STARTS HERE************

g) The Government’s Preparation for the “Lehman Weekend” Meetings at the FRBNY

The FRBNY, Treasury Department, the SEC and the Federal Reserve coordinated actions in what became known as the “Lehman Weekend” meetings of September 12-

14, 2008, at the FRBNY, in which the Government attempted to orchestrate a private sector rescue of Lehman.

On Wednesday, September 10, 2008, FRBNY staff put together a draft gameplan for a "liquidity consortium" of major Wall Street banks to "provide a forum where these firms can explore possibilities of joint funding mechanisms to avert Lehman's insolvency."[5889] Although a draft, the staff's proposed gameplan is an instructive, contemporaneous record of the thinking of some in the FRBNY with respect to how to approach Lehman during the uncertain week of September 8, 2008.

The draft gameplan contemplated that the meeting would occur "at the very latest" on Friday the 12th.[5890] Consortium members would be given "[v]ery little advance" notice, "2 hours max," in order to "minimize the risk of outside leaks."[5891] The gameplan further specified: "FRBNY to host. [Treasury Secretary Henry] Paulson delivers introductory remarks."[5892] Substantively, the gameplan provided that the officials from the assembled banks would be

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[5889] FRBNY, Liquidity Consortium (Sept. 10, 2008), at p. 1 [FRBNY to Exam. 003517]; e-mail from Michael Nelson, FRBNY, to Christine Cummings, FRBNY, *et al.* (Sept. 10, 2008) [FRBNY to Exam. 003516] (distributing Liquidity Consortium outline with the subject line, "revised liquidity gameplan"). Possible consortium members would include those depository and investment banks with exposures to Lehman through loans, triparty repos and derivatives; such firms would include: Citibank, Credit Suisse, Deutsche Bank, Goldman Sachs, Morgan Stanley, Merrill Lynch, JPMorgan, and the Royal Bank of Scotland. FRBNY, Liquidity Consortium (Sept. 10, 2008), at p. 1 [FRBNY to Exam. 003517].

[5890] *Id.*

[5891] *Id.*

[5892] *Id.* at p. 2.

> told by Paulson that they have until the opening of business in Asia (Sunday night N[ew] Y[ork] time) to explore whether they can jointly come up with a credible plan to recapitalize Lehman to an extent necessary to enable an orderly winding down. Paulson conveys willingness of the official sector to let Lehman fail.[5893]

The draft states that the FRBNY should fix a maximum amount that it would be willing to finance to the consortium, "but not divulge our willingness to do so to the consortium."[5894] Similarly, the draft states that the FRBNY must "hone in on the monetary figure we think the consortium will have to provide in new capital," as well as "the type/maximum amount of any FR [Federal Reserve] financing to support the consortium."[5895] Geithner later told the Examiner that any extension of Government funding to Lehman contemplated in the gameplan draft was contingent on Lehman having a willing buyer.[5896]

As of September 10, 2008, the FRBNY had settled on the public line that no government funds would be invested to rescue Lehman.[5897] This public line was a bargaining strategy to encourage a private consortium of banks to provide the funds themselves.[5898] The draft liquidation consortium gameplan, however, did not foreclose

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5893 *Id*.

5894 *Id*. at p. 2.

5895 *Id*. at p. 5.

5896 Examiner's Interview of Timothy F. Geithner, Nov. 24, 2009, at p. 9 (when shown the Liquidity Consortium gameplan document, Geithner confirmed that the FRBNY would have considered extending financing to Lehman, but only if a willing buyer for the firm had surfaced).

5897 Examiner's Interview of Thomas C. Baxter, Jr., Aug. 31, 2009, at p. 7.

5898 *Id*. (shown the Liquidity Consortium gameplan document, Baxter confirmed the Examiner's understanding that the references in the document to a "willingness" in the official sector to let Lehman the possibility that the FRBNY would finance some amount of liquidity; despite noting legal and fiscal obstacles in other areas, the draft did not raise any concern about the possibility of FRBNY financing.[5899] The gameplan slated the FRBNY to communicate with "foreign supervisors" on the evening of Friday September 12 while the consortium convened for its initial meeting.[5900]

A more detailed draft timeline for the implementation of the FRBNY's liquidation consortium plan was circulated the next morning, Thursday, September 11, 2008.[5901] The timeline provided that later in the morning Geithner would (1) inform Bernanke and Paulson that the FRBNY would convene the liquidity consortium on Friday; and (2) ask Paulson to make an introductory address to the group.[5902] Geithner would then contact BofA CEO Kenneth Lewis to probe BofA's interest in acquiring

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"fail," and the FRBNY's unwillingness to "divulge" the amount of financing it was willing to extend to the consortium was a "strategy" to encourage the gathered banks not to expect a "Bear Stearns solution," and thus to contribute their own funds to an industry solution to the Lehman problem).

[5899] The "Open Issues" section of the document identifies issues to be resolved in advance of the consortium meeting. FRBNY, Liquidity Consortium (Sept. 10, 2008), at pp. 2-3 [FRBNY to Exam. 003517]. These issues include: shareholder approval for any deal emerging from the meeting; the risk that creditors could put Lehman into involuntary bankruptcy prior to a resolution; and the need to obtain "[r]egulatory approvals," including from regulators outside of the United States. *Id.* Concern over legal authority or financial means to intervene to rescue Lehman is not present under the "Legal" sub-section of the draft agenda's "Open Issues" discussion. *Id.*

[5900] *Id.* at p. 2.

[5901] E-mail from Michael Nelson, FRBNY, to Christine Cumming, FRBNY (Sept. 11, 2008) [FRBNY to Exam. 003513] (cover e-mail); FRBNY, Timeline — Liquidation Consortium (Sept. 11, 2008) [FRBNY to Exam. 003514].

[5902] FRBNY, Timeline – Liquidation Consortium (Sept. 11, 2008), at p. 1 [FRBNY to Exam. 003514].

Lehman.[5903] If Lewis declined to make a bid on behalf of BofA, or if Lehman rejected the bid, the FRBNY would proceed with its consortium plan.[5904]

The September 11 draft timeline contemplated that the FRBNY would prepare the final list of consortium members on the evening of September 12, and settle on "minimum capital contributions expected from the consortium" as well as the "level" or "type of liquidity to be offered, if necessary, by the Federal Reserve."[5905] The timeline would have the FRBNY contact foreign regulators on the evening of September 12.[5906]

The timeline proposed that on Saturday and Sunday, after the consortium was convened, it would engage in due diligence on Lehman's assets in order to gauge the feasibility of any recapitalization plan, and report its progress to Bernanke, Paulson, and Geithner.[5907] If no plan was forthcoming, the FRBNY would "reach out to regulators in DC and abroad to inform them of potential market disruptions at the opening of business on Monday and/or possible bankruptcy filing by Lehman."[5908]

In his interview with the Examiner, FRBNY General Counsel Thomas Baxter described the Government's approach to the Lehman crisis succinctly. There were two possible models for Government intervention, Baxter explained: (1) the FRBNY could

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[5903] *Id*.
[5904] *Id*.
[5905] *Id*.
[5906] *Id*.
[5907] *Id*. at p. 2.
[5908] *Id*.

extend a "Maiden Lane" style non recourse loan to a potential purchaser of Lehman, as it did to JPMorgan with Bear Stearns;[5909] or (2) the FRBNY could convene a consortium of private market participants to finance Lehman's bad assets, as it had in the case of the near failure of the hedge fund Long Term Capital Management ("LTCM") in 1998.[5910] The goal, Baxter said, was to make Wall Street view the LTCM intervention, rather than the Bear Stearns intervention, as the model for Lehman.[5911]

The FRBNY's actions in the Bear Stearns rescue placed public funds at risk and stood in contrast to the FRBNY's approach to LTCM. LTCM was a hedge fund that had become over leveraged and was brought to the brink of collapse by market conditions caused by Russia's default on its debt obligations in 1998.[5912] The FRBNY feared that LTCM's creditors and counterparties would close out their positions, and liquidate collateral supporting those positions simultaneously. Such an *en masse* liquidation, the

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[5909] In order to contain the economic fallout of the Bear Stearns near collapse and to facilitate an acquisition of the failed investment bank by JPMorgan, on March 16, 2008, the Federal Reserve Board of Governors granted the FRBNY authority to extend a $29 billion senior loan to a newly-created Delaware LLC called "Maiden Lane." JPMorgan also extended a $1 billion subordinated note to Maiden Lane. Maiden Lane, in turn, purchased $30 billion of illiquid assets from Bear Stearns, as marked-to-market by Bear on March 14, 2008. The transfer involved $30 billion in illiquid real estate-related assets from Bear Stearns to Maiden Lane. Because the FRBNY loan was styled as a non-recourse loan, the FRBNY's commitment was secured only by the portfolio of assets held by Maiden Lane. Thus the U.S. Government was responsible for any losses in the event the liquidation of the transferred assets could not fully repay the principal advanced by the FRBNY. *See* FRBNY, Press Release: Summary of Terms and Conditions Regarding the JPMorgan Facility (Mar. 24, 2008), *available at* http://newyorkfed.org/newsevents/news/markets/2008/rp080324b.html.

[5910] Examiner's Interview of Thomas C. Baxter, Jr., Aug. 31, 2009, at p. 8.

[5911] *Id*.

[5912] General Accounting Office, *Long-Term Capital Management: Regulators Need to Focus Greater Attention on Systemic Risk*, Report to Congressional Requesters (Oct. 29, 1999), at 42.

FRBNY believed, would result in "a likelihood that a number of credit and interest rate markets would experience extreme price moves and possibly cease to function for a period of one or more days and maybe longer."[5913] After remedies short of Government intervention had failed, the FRBNY convened a consortium of LTCM's major creditors to devise an industry created plan to recapitalize the hedge fund. Thus, on September 22 and 23, 1998, 14 banks and securities firms met at the FRBNY's offices, created a term sheet for a recapitalization of the hedge fund and, ultimately, committed to inject $3.6 billion in LTCM to avoid a disorderly liquidation.[5914] As former FRBNY President William McDonough emphasized in his testimony before the U.S. House of Representatives: "[T]his was a private sector solution to a private sector problem, involving an investment of new equity by Long Term Capital's creditors and counterparties."[5915]

Rather than a Bear Stearns style "bailout" for Lehman,[5916] the FRBNY went forward with plans for a LTCM style "liquidation consortium" on September 12, 2008.

[5913] Statement by William J. McDonough, President of the Federal Reserve Bank of New York Before the Comm. on Banking and Financial Servs., U.S. House of Representatives, Oct. 1, 1998, at 4.
[5914] *Id*. at pp. 6-7; GAO Report to Congressional Requesters, Long-Term Capital Management: Regulators Need to Focus Greater Attention on Systemic Risk (Oct. 29, 1999), at 44.
[5915] Statement by William J. McDonough, President of the Federal Reserve Bank of New York Before the Comm. on Banking and Fin. Servs., U.S. House of Representatives, Oct. 1, 1998, at p. 7.
[5916] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 9.

h) On the Evening of Friday, September 12, 2008, the Government Convened a Meeting of the Major Wall Street Firms in an Attempt to Facilitate the Rescue of Lehman

By all accounts, the liquidation consortium meetings at the FRBNY began largely as conceived in the draft agenda and timelines. The FRBNY convened a meeting of the major Wall Street financial institutions, all of which agreed to finance Lehman's bad assets and thereby facilitate the sale of Lehman to one of its suitors.[5917] However, the deal foundered on the issue of whether Barclays would be able to guarantee Lehman's outstanding trades, as requested by the FRBNY.

True to the FRBNY's draft gameplan, Geithner spoke with Callum McCarthy, then Chairman of the British Financial Services Authority ("FSA") on September 11, and informed McCarthy of FRBNY plans to convene "a consortium of financial institutions . . . to rescue Lehman."[5918]

During the morning of September 12, 2008, John S. Varley, Group Chief Executive of Barclays, spoke with Paulson.[5919] Varley informed Paulson that Barclays was interested in making a bid for Lehman.[5920] Paulson responded that any purchaser would need to make a bid before the end of the weekend, after which time the

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[5917] *Id*. at pp. 9-10.
[5918] Financial Services Authority (U.K.), Statement of the Financial Services Authority (Jan. 20, 2010), at p. 2.
[5919] *Id*. at p. 3.
[5920] *Id*.

Government planned to place Lehman into an orderly wind down.[5921] According to the FSA, in a conversation later that day, Alistair M. Darling, Chancellor of the Exchequer, advised Paulson "that no transaction with Barclays would be possible if the level of risk to Barclays was inappropriate."[5922] Paulson "accepted this and advised that the FRBNY might be prepared to provide Barclays with regulatory assistance to support such a transaction if it was required."[5923]

On the evening of Friday, September 12, 12 investment bank CEOs were summoned to the FRBNY's headquarters at 33 Liberty Street in New York City.[5924] Bernanke remained in Washington, given the possibility that the Federal Reserve might need to exercise its emergency lending powers, which would require him to convene a Federal Reserve Board meeting.[5925] The CEO participants present at 33 Liberty included: JPMorgan's Jamie Dimon, Morgan Stanley's John Mack, Citigroup's Vikram Pandit and Robert Wolf of UBS. Executives from Lehman Brothers did not attend.[5926]

Paulson opened the meeting by noting the absence of Lehman representatives.[5927] Paulson said their absence was intentional, because the meeting was convened to

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[5921] *Id*.
[5922] *Id*. at p. 5.
[5923] *Id*.
[5924] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 9.
[5925] Examiner's Interview of Ben S. Bernanke, Dec. 22, 2009, at p. 9.
[5926] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 9.
[5927] *Id*.

discuss Lehman specifically.[5928] Paulson noted the absence of BofA and Barclays Capital executives as well, due to the fact that these banks were involved in potential deals to acquire Lehman.[5929]

Paulson stated that the purpose of the meeting was twofold. First, the Government tasked the CEOs with creating a plan to facilitate the acquisition of Lehman, and second, if such a plan was not forthcoming, Paulson stated the onus was on the CEOs to provide the Government with the means to resolve the consequences of Lehman's failure.[5930] Moreover, with regard to the financing of any potential rescue of Lehman, Paulson stated: "Not one penny will come from the Government."[5931] Paulson did not elaborate, but Lehman's only options were to be rescued by a firm (or a consortium of firms) or to file for bankruptcy on Monday, September 15.[5932]

Secretary Paulson told the Examiner that no Government aid would be forthcoming because he concluded that the Government lacked authority to inject capital into struggling institutions.[5933] While Paulson allowed that under Section 13(3)

[5928] *Id*.

[5929] Examiner's Interview of Henry M. Paulson, Jr., June 25, 2009, at pp. 15-16.

[5930] *Id*. at p. 16.

[5931] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 9 (reporting Paulson's statement).

[5932] *Id.* Cox said that most attendees "probably assumed that [Secretary Paulson's statement of no government help] was a negotiation" strategy and were "generally surprised when in fact there was no money there." Examiner's Interview of Christopher Cox, Jan. 8, 2010, at p. 15.

[5933] Examiner's Interview of Henry M. Paulson, Jr., June 25, 2009, at p. 16.

of the Federal Reserve Act the Fed might be able to lend against any collateral,[5934] he feared that providing emergency funds to the ailing bank would cause its clients to flee, ensuring its demise.[5935]

That weekend, Lehman's "financial team" came on site to the FRBNY and "opened their books" to representatives from the investment banks in order to work out the details of any potential rescue.[5936] Barclays was permitted to examine Lehman's books, in order to conduct the due diligence necessary to determine whether it would acquire Lehman.[5937] Baxter noted concern among the firms that by negotiating a rescue for Lehman, they would be "financing a sweetheart deal for one of their competitors."[5938] Nevertheless, due diligence and planning continued.

But Barclays and the British regulators had their own reservations. During the evening of September 13, 2008, Barclays advised the FSA that the FRBNY was asking Barclays to guarantee Lehman's financial obligations in a manner similar to that

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5934 Section 13(3) provides that a Federal Reserve Bank may, "[i]n unusual and exigent circumstances" lend to any individual or corporation so long as the lending is "secured to the satisfaction" of the Federal Reserve Bank. 12 U.S.C. § 343. But the Fed and FRBNY emphasized that they could not lend against insufficient collateral. Examiner's Interview of Ben S. Bernanke, December 22, 2009, at 2 (then-FRBNY President Timothy F. Geithner informed Chairman Bernanke that the Fed would be "lending into a run," and that, while a loan might help pay off some counterparties, it would not save Lehman. Chairman Bernanke concluded that Lehman was insolvent and lacked any collateral, given that its assets fell short of obligations that would come due).

5935 Examiner's Interview of Henry M. Paulson, Jr., June 25, 2009, at p. 16.

5936 Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at pp. 9-10.

5937 Financial Services Authority (U.K.), Statement of the Financial Services Authority (Jan. 20, 2010), at p. 5.

5938 Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 10.

provided by JPMorgan when it acquired Bear Stearns.[5939] Barclays recognized, and the FSA confirmed, that British regulations would require shareholder approval before such a guaranty could be granted.[5940] Later that evening, Barclays advised the FSA that "because of the guarantee" issue, it was "unlikely that a suitable structure to purchase Lehman could be put in place which would satisfy [its] Board."[5941] McCarthy spoke to Geithner that evening about the state of the negotiations, and McCarthy reported that although no proposal had yet been shown to the FSA by Barclays, "if one was it would raise significant issues."[5942] Yet, because no proposal had "been put forward . . . it was impossible to say whether any particular proposal would prove acceptable."[5943]

On the afternoon of Sunday, September 14, 2008 (London time), the FSA informed the FRBNY that the guaranty issue would need to be resolved before any take over could be approved.[5944] According to the FSA, Geithner replied that the FRBNY had arranged for a consortium of Wall Street firms to take Lehman's illiquid assets, but that a guaranty from Barclays "would still be required."[5945] Barclays, the FSA

[5939] Financial Services Authority (U.K.), Statement of the Financial Services Authority (Jan. 20, 2010), at p. 7.

[5940] *Id*.

[5941] *Id*.

[5942] *Id*.

[5943] *Id*.

[5944] *Id.* at p. 8. Baxter advised the Examiner that the FRBNY did not learn that providing a guaranty had become an issue until "late" on Sunday, September 14. Examiner's Interview of Thomas C. Baxter, Jr., Aug. 31, 2009, at p. 8.

[5945] Financial Services Authority (U.K.), Statement of the Financial Services Authority (Jan. 20, 2010), at p. 8.

and the FRBNY continued to discuss the regulatory and prudential obstacles presented by the guaranty issue throughout the day on September 14. By late afternoon or early evening, however the FSA and Barclays "agreed that neither the Barclays Board nor the FSA could approve any transaction structure that required Barclays to provide the guarantee asked for by the FRBNY."[5946]

Over the weekend, the assembled banks had agreed to provide at least $20 billion in financing to facilitate Lehman's acquisition by Barclays.[5947] According to Government witnesses, it was not for want of cooperation, coordination or Government pressure that Lehman was not acquired.[5948] Rather, those Government representatives present for the meetings laid the failure of the deal on Barclays' inability to guarantee trading losses associated with the acquisition.[5949]

Baxter was clear in his conviction that the inability of Barclays to obtain a guaranty was due to the unwillingness of the British government, specifically the FSA, to waive the British legal requirement that Barclays obtain a shareholder vote on the issue.[5950] This critical viewpoint was uniformly held among the FRBNY witnesses interviewed by the Examiner. Voigts agreed that a sale of Lehman was not possible because Barclays was unable to obtain a waiver from the FSA to guarantee Lehman's

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[5946] *Id*. at p. 10.
[5947] Examiner's Interview of Henry M. Paulson, June 25, 2009, at p. 18.
[5948] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 9.
[5949] *Id*.; Examiner's Interview of Jan H. Voigts, Aug. 25, 2009, at p. 7.
[5950] Examiner's Interview of Thomas C. Baxter, Jr., Aug. 31, 2009, at p. 8.

obligations.[5951] Geithner echoed these comments, stating that a deal during Lehman Weekend was impracticable because Lehman lacked a buyer.[5952] In Geithner's view, had Lehman had a buyer in Barclays or any other third party, the Government would have extended financing to that buyer to help facilitate the sale.[5953] Bernanke also attributed the Government's ultimate inability to rescue Lehman to the absence of a buyer for the firm.[5954]

Baxter stated his belief that the British government simply did not want Barclays to acquire Lehman, and therefore refused to allow Barclays to guarantee the deal, or otherwise backstop the transaction.[5955] The FSA explained to the Examiner that, because Barclays was one of the U.K.'s clearing banks, "it was important to ensure that Barclays did not expose itself to a level of risk that would weaken it to an extent that could have a wider systemic impact on the U.K. financial system."[5956] Further, Chairman McCarthy told Chairman Cox that there was no precedent for waiving the U.K. law requirement that Barclays obtain shareholder approval prior to agreeing to any guaranty in these

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5951 Examiner's Interview of Jan H. Voigts, Aug. 25, 2009, at p. 7.
5952 Examiner's Interview of Timothy F. Geithner, Nov. 24, 2009, at p. 9.
5953 *Id*.
5954 Examiner's Interview of Ben S. Bernanke, Dec. 22, 2009, at p. 2.
5955 Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 10.
5956 The Examiner sought, but was not granted, an interview with the FSA decision makers; but the FSA did provide written answers to questions. Financial Services Authority (U.K.), Statement of the Financial Services Authority (Jan. 20, 2010), at p. 6.

exigent circumstances.[5957] Cox indirectly confirmed to the Examiner that the FSA acted reasonably.[5958] For his part, Baxter stated that there was a "policy issue" with the FRBNY providing a backstop for an acquisition by a British bank.[5959] Baxter said that the FRBNY lacked this authority because the FRBNY could not issue a guaranty to support the transaction.[5960] Rather, the FRBNY could only provide secured financing in support of such a transaction.[5961] Baxter stated that he found it "shocking" that the deal would founder for lack of a guaranty, and that it was the financing of the deal, rather than the guaranty which should have been the most challenging barrier to overcome in any rescue of Lehman.[5962]

Paulson distinguished the Government's action to intervene to backstop AIG, from the absence of Government action to backstop Lehman. According to Paulson, Lehman had liquidity problems and no hard assets against which to lend.[5963] AIG, by contrast, Paulson said, had a capital problem at the holding company level, but

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[5957] *Id*. at p. 10.

[5958] Examiner's Interview of Christopher Cox, Jan. 8, 2010, at p. 18. (Cox recalled a specific conversation on the subject, but after SEC counsel would not permit him to recount that conversation, invoking the "deliberative process" privilege, Cox answered the general question: "In all your conversations with the FSA, did they ever take an unreasonable position?" Chairman Cox responded: "At no time in my dealings with the FSA did I think they were unreasonable; they had reasons for what they did.").

[5959] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 10.

[5960] *Id*.

[5961] *Id*.

[5962] *Id*.

[5963] Examiner's Interview of Henry M. Paulson, Jr., June 25, 2009, at p. 16.

otherwise had regulated insurance companies that were perceived by the market as stable, well capitalized, and having real value.[5964]

A bankruptcy filing by the holding company was another of the contingency plans discussed at the FRBNY that weekend.[5965] The Government concluded that an *en masse* liquidation of the holding company would be "awful," and should be avoided.[5966] Nevertheless, assuming no alternative was available, the plan envisioned by the Government would be for LBHI to file for Chapter 11, while JPMorgan continued to lend to LBI as a going concern. LBI would then be eased into a SIPA proceeding, and wound down in an orderly way.[5967] This plan did not play out once Barclays came back to the bargaining table with a proposal to acquire the broker dealer after LBHI entered bankruptcy.

On Sunday September 14, Baxter and Cox participated in a conference call with Lehman's Board of Directors.[5968] Also present on the Government side of the call were SEC General Counsel Brian Cartwright and Alan Beller of Cleary Gottlieb Steen & Hamilton, who was engaged by the Treasury Department.[5969] Baxter said the call was

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5964 *Id*.
5965 Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 10.
5966 *Id*.
5967 *Id.* at pp. 10-11.
5968 Lehman Brothers Holdings Inc., Minutes of Meeting of Board of Directors (Sept. 14, 2008) [LBEX-AM 003932] (noting that Baxter and Cox addressed the Board by telephone).
5969 Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 10.

arranged at the request of Paulson and Geithner.[5970] According to Lehman Board minutes, Baxter and Cox emphasized that the Board needed to make a decision regarding whether to file for bankruptcy quickly, and that this was a decision for the Board alone.[5971] Baxter recalled making statements to this effect.[5972] Cox recalled that he did not mention bankruptcy, but rather stated that whatever decision Lehman might make needed to be made immediately.[5973] Cox also recalled that "others from the Fed" who were on the call added that the Government had made it clear in earlier meetings that Lehman should file for bankruptcy.[5974] Baxter said he made the point "that opening on Monday was not an option because of the chaos in the markets."[5975]

Also that evening, the Federal Reserve broadened the collateral eligible for financing through the PDCF "to closely match the types of collateral that can be pledged in the triparty repo systems of the two major clearing banks."[5976] However, the FRBNY limited the collateral LBI could use for overnight financing to the collateral that

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[5970] *Id*.

[5971] Lehman Brothers Holdings Inc., Minutes of Meeting of Board of Directors (Sept. 14, 2008), at pp. 5-6 [LBEX-AM 003932].

[5972] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 11.

[5973] Examiner's Interview of Christopher Cox, Jan. 8, 2010, at p. 17.

[5974] *Id*.

[5975] Lehman Brothers Holdings Inc., Minutes of the Meeting of the Board of Directors (Sept. 14, 2008), at pp. 5-6 [LBEX-AM 003932]; Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 10.

[5976] FRBNY, Press Release (Sept. 14, 2008), *available at* http://www.federalreserve.gov/newsevents/press/monetary/20080914a.htm.

was in LBI's box at JPMorgan as of Friday, September 12, 2008.[5977] This restriction was referred to as the "Friday criteri[on]."[5978] In addition, the FRBNY imposed larger haircuts on LBI's PDCF borrowing than it did on other investment banks,[5979] and the haircuts imposed on LBI's PDCF borrowing were larger than under Lehman's pre bankruptcy triparty borrowing.[5980]

In connection with Lehman's preparations to file the LBHI Chapter 11 petition, the FRBNY, acting as a lender of last resort, advised Lehman that it would provide up

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5977 Examiner's Interview of Robert Azerad, Sept. 23, 2009, at p. 5; Examiner's Interview of Christopher Burke, July 7, 2009, at p. 3. An experimental allocation by Lehman to the PDCF on Monday morning showed at least $72 billion of eligible Lehman securities being swept into the PDCF system. *See* e-mail from John N. Palchynsky, Lehman, to Craig L. Jones, Lehman, *et al.* (Sept. 15, 2008) [LBEX-DOCID 076981];. *see also* Lehman, PDCF Schedule of Eligible Securities (Sept. 14, 2008) [LBEX-DOCID 405695].

5978 Examiner's Interview of Robert Azerad, Sept. 23, 2009, at p. 5; Examiner's Interview of Christopher Burke, July 7, 2009, at p. 3. According to Azerad, this restriction prevented Lehman from posting the range of collateral to the PDCF that other firms were allowed to post after September 15, 2008. Examiner's Interview of Robert Azerad, Sept. 23, 2009, at p. 5; *see also* e-mail from Timothy Lyons, Lehman, to Ian T. Lowitt, Lehman (Sept. 14, 2008) [LBEX-DOCID 070210] (stating "the fed is letting the other eighteen broker dealers fund a much broader range of collateral than us").

5979 Examiner's Interview of Christopher Burke, July 7, 2009, at p. 3; *see also* e-mail from Ricardo S. Chiavenato, JPMorgan, to Christopher Carlin, JPMorgan, *et al.* (Sept. 15, 2008) [JPM-2004 0055329]; Examiner's Interview of Robert Azerad, Sept. 23, 2009, at p. 5. According to Azerad, the Fed imposed the wider haircuts on Lehman because the Fed was not willing to take any losses in its overnight financing of Lehman. *Id.*

5980 *See* e-mail from Sindy Aprigliano, Lehman, to Paolo R. Tonucci, Lehman, *et al.* (Sept. 15, 2008) [LBEX-DOCID 4572426, 4579671] (attaching list of an estimated haircut impact of approximately $4 billion); e-mail from Sindy Aprigliano, Lehman, to George Van Schaick, Lehman, *et al.* (Sept. 15, 2008) [LBEX-DOCID 077028] (discussing the larger haircuts imposed by the Fed on Lehman's PDCF borrowing); e-mail from Robert Azerad, Lehman, to Susan McLaughlin, Lehman, *et al*. (Sept. 15, 2008) [LBEX-DOCID 457643] (explaining the PDCF haircuts would "result in a $4 billion drain in liquidity . . . ."); *see also* Lehman, PDCF Schedule of Eligible Securities (Sept. 14, 2008) [LBEX-DOCID 405695] (detailing the PDCF haircuts applied to Lehman for the various categories of accepted securities); e-mail from Ricardo S. Chiavenato, JPMorgan, to Christopher Carlin, JPMorgan, *et al*. (Sept. 15, 2008) [JPM-2004 0055329]. *But see* e-mail from Sindy Aprigliano, Lehman, to Paolo R. Tonucci, Lehman, *et al.* (Sept. 15, 2008) [LBEX-DOCID 068353] (stating the haircut impact from using the PDCF would be $2 billion).

to two weeks of overnight secured financing through the PDCF to allow LBI to accomplish an orderly liquidation.[5981]

Baxter rejected the idea that "moral hazard" arguments played a role in "allowing" Lehman to fail. Baxter said the whole purpose of the FRBNY's extraordinary actions that weekend was to rescue Lehman in some form:[5982] "In no way was the idea to make Lehman a 'poster child' for moral hazard."[5983] "Clearly," Baxter said, "my sense was that [the Government] was not just going through the motions" and that Lehman was not "sacrificed to moral hazard."[5984] Baxter attributed the failure of the rescue effort to the British government's refusal to offer a guaranty to backstop the acquisition.[5985] In his interview, Paulson said that although economic health depends on Wall Street firms believing that the Government cannot and will not rescue them in a crisis, economic stability was nevertheless more important to the economy than moral hazard.[5986]

5981 Examiner's Interview of Shari D. Leventhal, Apr. 30, 2009, at pp. 4-5. Some FRBNY employees thought the FRBNY was risking too much exposure with the two-week funding timeframe. *Id.* at p. 5.

5982 *Id*.

5983 *Id*.

5984 *Id*.

5985 *Id.* There were two distinct issues: (1) The U.K. regulators' refusal to waive the shareholder vote requirement necessary to approve a Barclays guaranty of outstanding Lehman trades; and (2) Lehman's failure to obtain a guaranty from Barclays, or any other entity, for potential trading losses.

5986 Examiner's Interview of Henry M. Paulson, Jr., June 25, 2009, at p. 22.

i) Lehman's Bankruptcy Filing

LBHI filed for bankruptcy protection on Monday, September 15. The FRBNY was surprised by the consequences that Lehman's filing had in terms of funding LBIE, which was taken into administration by British regulators due to inadequate capitalization.[5987] The FRBNY was unaware that LBIE was financed entirely by the parent that is, that LBHI pulled liquidity into New York, and would then re route that funding to LBIE in the U.K.[5988] Baxter said he was unaware until that Monday that LBIE was dependent on its LBHI parent, but he learned otherwise when LBHI was forced to file for bankruptcy due to cross defaults from LBIE going into administration in the U.K.[5989] Even then, Baxter assumed that the Bank of England had the capacity to fund LBIE in a manner similar to that by which the FRBNY funded LBI through the Primary Dealer Credit Facility discount window for broker dealers.[5990] The FSA told the Examiner that once it became known that LBHI would file for bankruptcy, the FSA asked the FRBNY if financing (via the FRBNY's discount window for broker dealers) would be made available to LBIE and was told that it would not.[5991]

[5987] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 11; Examiner's Interview of Jan H. Voigts, Aug. 25, 2009, at pp. 7-8 (noting surprise at the extent to which LBIE was dependent on LBHI, the consequences of LBHI's bankruptcy, and the importance and complexity of intercompany funding within Lehman generally).

[5988] Examiner's Interview of Thomas C. Baxter, Jr., May 20, 2009, at p. 11.

[5989] *Id*.

[5990] *Id*.

[5991] Financial Services Authority (U.K.), Statement of the Financial Services Authority (Jan. 20, 2010), at pp. 10-11.

Following Lehman's bankruptcy, Lehman, through its broker dealer, LBI, relied on the PDCF to obtain $40 to $50 billion in overnight financing needed to repay its clearing banks.[5992] In addition, Lehman funded itself after the bankruptcy filing through two other FRBNY programs, the Open Market Operations ("OMO") and the Term Securities Lending Facility ("TSLF"),[5993] as well as triparty term repos that had not yet expired.[5994] The FRBNY's overnight financing of LBI began Monday evening, September 15, with Lehman borrowing approximately $28 billion via the PDCF.[5995] The FRBNY's overnight financing continued through Thursday morning, September 18, 2008.[5996] LBI was placed into SIPA proceedings on September 19, 2008.

[5992] *See* e-mail from David A. Weisbrod, JPMorgan, to Jamie L. Dimon, JPMorgan, *et. al*. (Sept. 15, 2008) [JPM-2004 0080146] (listing Lehman's triparty repo borrowing at $51 billion ($28 billion from the PDCF, $2 billion from Barclays, and $21 billion from other investors) for Monday); Alvarez & Marsal, Summary of Meeting with James Hraska on 10/08/08 [Draft] (Oct. 8, 2008), at pp. 1-4 [LBEX-AM 003302] (listing the Fed's funding of Lehman (via the PDCF, OMO, and TSLF) for the week following the LBHI petition).

[5993] Examiner's Interview of Christopher Burke, July 7, 2009, at p. 4; Alvarez & Marsal, Summary of Meeting with James Hraska on 10/08/08 [Draft] (Oct. 8, 2008), at pp. 1-4 [LBEX-AM 003302].

[5994] *See* e-mail from David A. Weisbrod, JPMorgan, to Jamie L. Dimon, JPMorgan, *et. al*. (Sept. 15, 2008) [JPM-2004 0080146-47] (listing $21 billion in "mainly term repos" as part of LBI's triparty borrowing for September 15).

[5995] *See* e-mail from Edward J. Corral, JPMorgan, to William Walsh, JPMorgan, *et al.* (Sept. 15, 2008) [JPM-2004 0031195] (notifying the Fed that the Lehman assets used in LBI's $28 billion PDCF repo on Monday night satisfied the Friday criterion). Earlier on Monday, Lehman estimated that it would borrow up to $35 billion through the PDCF on Monday night. *See* e-mail from Sindy Aprigliano, Lehman, to Robert Azerad, Lehman (Sept. 15, 2008) [LBEX-DOCID 1071653] (providing John Feraca's PDCF estimate of $27 billion plus a buffer of $8 billion); e-mail from Robert Azerad, Lehman, to Susan McLaughlin, Lehman, *et al.* (Sept. 15, 2008) [LBEX-DOCID 071550] (estimating $34 billion of PDCF borrowing); e-mail from Paolo R. Tonucci, Lehman, to Susan McLaughlin, Lehman, *et al.* (Sept. 15, 2008) [LBEX-DOCID 071550] (estimating $28.3 billion for the collateral value of the PDCF borrowing).

[5996] Examiner's Interview of Robert Azerad, Apr. 20, 2009, at p. 5.