MEMORANDUM FOR THE RECORD

Event: Interview with Erin Callan, Former CFO of Lehman Brothers

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Team Leader: Jay Lerner

Location: FCIC small conference room

Participants - Non-Commission:

- Erin Callan
- Dietrich Snell, Proskauer
- Seth D. Fier, Proskauer

Participants - Commission:

- Jay Lerner
- Troy Burrus
- Sarah Knaus

MFR Prepared by: Sarah Knaus (reviewed by Julia Lanzara)

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Summary of the Interview or Submission:

This is a paraphrasing of the interview dialogue and is not a transcript and should not be quoted as such.

Burrus: Thank you for taking the time to meet with us. We are from the FCIC, which is a legislative commission put together in 2009 to investigate the causes of the financial crisis. As part of that, we're looking into different factors and looking into various companies. We (Jay and Troy) are looking at Lehman Brothers, which is how your name came up. We're going to ask you questions about the topics I sent to you. We're here to get your side of the story and ask you questions. You're purely a witness. We just want to get your impressions and information. If at any time you have questions, please stop us. It's basically an informal interview. First, I'd like to have your educational background:

Callan: I graduated from Harvard with honors in 1987. I graduated from NYU law in 1990, after which I joined Simpson, Thacher, Bartlett from 1990 to 1995. My specialization was corporate taxation. In that context I worked with Lehman, a client of the firm. I started at Lehman in 1995, where I stayed until I resigned in 2008.

Burrus: When you started at Lehman what was your role?

It was pretty specialized, I worked on a team responsible for raising preferred stock for clients. I was working on regulatory capital issues, rating agency issues, and accounting issues, because it was right around the time that trust preferred securities were released. These were the new frontier. Their release qualified as bank capital by the Fed. I spent my time with banks across the country and globe, working on ways to raise capital. This is what I ultimately did for most of my career. A lot in financial institutions, raising capital, forms of capital.

Burrus: How long did you do that?

Callan: For a few years I did that, then I moved into a role where I was responsible for debt capital markets, and was responsible for raising debt capital. Then I was asked to run the entire capital raising effort, starting in 1998. Over time there was a bleeding out of expansion of my role and I became responsible for any capital raising efforts for clients. Any new or different way, any tailored or bespoke. By the end of that whole cycle this had become the Product Development Group, New Products Group. It was advisory in nature, and wasn't on the investment banking side of the business. I did this until 2006, when they asked me to head up an investment banking advisory effort for hedge fund clients, who had always before been treated as trading partners, but they were becoming more like asset management companies. I could advise these companies about how to be mature investment institutions. Very successful effort, took Blackstone and Oxsif public. I was asked to take the CFO role in February 2007, but it was not publically announced or started operating with any information until late September 2007.

Burrus: Who came to you and asked you?

Callan: Joe Gregory.

Burrus: Did they explain why you?

Callan: Yes. I wasn't actually very excited about it when it was presented, but not because of the environment, but more about the job. At least as I had observed it in the firm, it wasn't something that was very meaningful. But, what was articulated to me, by Joe, was that they were looking for the job to be different, more impactful, there was the notion that I could translate my skills in terms of my experience in raising capital and understanding strategically for clients, that I could do it for our firm. And I was articulate, with great communication skills and contacts up and down the business side of the firm. I could be strategic about the role from the business side of the firm, which was unique.

Lerner: Was Mr. Gregory unhappy with O'Meara?

Callan: He never said anything to me. I asked, as would be prudent, do you think Chris failed? There was never any suggestion that he failed or anything said to me indirectly or directly made me think that. Not some desire that Chris was underperforming.

Lerner: Why do you think they were making the change?

Lawyer: When you're asking questions like that you just want her interpretations?

Callan: I didn't really know what was going on. I was asked in February and I ruminated on it because I was thinking of running a big business at that point. Once I accepted, pretty quickly thereafter, it was a locked down secret, because it was unclear at what point it would be announced. I wasn't allowed to talk to anybody about it. I was running a successful business at the time, and they wanted to keep me focused until they could make the change. I was aware of what was going to happen, Chris was to take Madelyn's role, and Madelyn was going to take a policy role. At the time, I wasn't part of the executive suite, I was on the trading floor and I just didn't get a lot of information about it. I knew what the musical chairs would be, but nobody really came back to me, and the people I spent every day with didn't know anything about it.

Lerner: Why did they want to make the CFO position more impactful or have more gravitas?

Callan: Nobody said why, but I could imagine why.

Lerner: What did you imagine?

Callan: I think we had been a firm without a real face, and people didn't know much about the firm. We'd been pretty quiet. We shied away the press and wasn't sort of better known in the bigger picture. I thought it was time to be more out there about the firm and the culture. That's what I made up. The firm was becoming global; it expanded dramatically away from fixed income business, we had developed a real investment banking presence. The firm was advancing to being more fully developed. I kind of assumed this is one of the areas you think about.

Lerner: Was there an event that led to the greater maturation and global presence during that time frame in 2006ish?

Callan: I just know as any other employee. I started to sense that there had been a lot of success. The firm had been pretty one-dimensional. Why not leverage that success into other businesses.

We expanded into equities in Europe and Asia, etc. I don't know what precipitated that, other than the success.

Lerner: Did you have any other indications about the firm taking a more external face, any other indications?

Callan: I mean I had a sense that there was a pretty active branding strategy, but I wasn't a part of it, there was some energy put into it. There was a tag line – "where vision gets built." Or we would have a new mantra screensaver, the big brother type of stuff. Now we're bigger, more global, time for a brand strategy. This is all speculation

Lerner: Were other investment banks doing the same thing?

Callan: Observationally, yes, but Lehman was still pretty small, albeit bigger than Bear. This was a little bit of catch up.

Burrus: When you took the CFO role, who did you report to?

Callan: I reported to Ian Lowett in the administrative reporting line, which was never clear as to what it meant, but it was important psychologically. I reported to Dick and Joe. Chris O'Meara also reported this way as CRO.

Burrus: Let's talk about leverage, I don't know if you've read any of the Valukas report, but they say they interviewed you in October 2009. It seems like there was a big importance in reducing leverage, during your time as CFO, why?

Callan: A tale of two cities.

Lerner: How did it evolve or change?

Callan: I took the role December 1. At that point, during 1Q there was very little emphasis on delivering, but not a lot of traction on it. There's some comment in the Examiner's Report about that. I was very vocal from early in my tenure about taking the leverage down. Leverage is relevant in terms of the types of assets. The absolute leverage number doesn't mean anything unless you understand the liquidity profile of the assets. I talk a lot in emails about the leverage in our illiquid assets portfolio. If you had treasuries, you could have higher leverage. Illiquid assets are a lot different. Speaking about de-levering, it is in the same time as selling off illiquid assets. What I started with from the beginning, because I got an opportunity, was to hear what people were concerned about. This was a great opportunity, because I didn't make any of the decisions and couldn't be held responsible. Investors could be very open with me. Feedback was consistent about the real estate exposure of the firm, both residential and commercial. In late January I started to talk to Dick and Joe about the need to get the leverage down. Most important was taking down the illiquid asset classes. It didn't get a lot of traction at that point. I didn't have the authority in my role to enforce the outcome. I couldn't just say that I would sell off those assets. I needed Joe particularly to give that directive. That didn't really change until early March.

Lerner: Why do you think you weren't getting traction?

Callan: The businesses wouldn't want to stand up and sell the assets. It required a real top-down directive. It wasn't going to bubble up, it was going to need to be mandated from up above. My own speculation is that no one ever disagreed, but nothing ever really happened to enforce it. At the time, there were no consequences for the failure to accomplish it. Why do I think nobody decided we needed a harsh directive? I saw a lot of plans about taking down the exposure to commercial real estate. It was in the 18th draft when I took the seat. I think people were hoping things would get better and it wasn't really necessary, maybe it wasn't going to be a contagion across asset classes. Maybe if we wait a bit longer.

Lerner: Do you remember specific conversations with Dick and Joe?

Callan: Yes, there was never any pushback. I just couldn't get wheels in motion to require them to happen. Ultimately that didn't really happen until March, where you may look at a confluence of events, there was a recognition that this needed to happen.

Lerner: You mentioned there had been plans, when did that start or how did it come about?

Callan: I don't know when it started, but during the exec committee meeting in December the real estate team presented a game plan on how to reduce the exposure. This was an updated version of the game plan. My sense was there were other plans, but I'm not sure why I thought that.

Lerner: Did they give any background as to why it was created in the first place or why it was being presented?

Callan: I can't say for sure, but my sense was that it was understood that there was more real estate exposure on the balance sheet than they had planned for. There were already assets that had been securitized. In that context of having a big balance sheet exposure, there was a desire to learn how to take it down.

Lerner: At the exec committee meeting, did Dick or Joe had any sort of response?

Callan: I don't remember it as active Q and A, but usually there'd be a presentation and a limited number of questions and then you'd move to the next topic. It would be unusual if they hadn't been familiar with the presentation. Joe was responsible for the exec com meetings. Usually, he would have vetted the flavor of the topic and presentation beforehand. Usually the presentation would have been sent to him.

Lerner: And they weren't willing to make a directive?

Callan: I didn't interpret it as the real estate group was warning them. Just to clarify, the way I saw it was they'd been asked to tell how they were going to get it down. They weren't necessarily worried, they were told "you have a lot of exposure and tell us your plan." There didn't seem to be any consequences for failing to execute on the plan, but Dick or Joe told them they needed a plan.

Lerner: Who presented?

Callan: Mark Walsh. He was in charge of Commercial.

Lerner: There was a reference to GREG?

Callan: The Global Real Estate Group.

Burrus: Was this topic discussed in March exec com meeting?

Callan: In March, I was getting more and more alarmed that we made it through 1Q and sold off some leveraged loan exposure, but hadn't done anything material with real estate. What became our Achilles heel was our real estate exposure. I knew from my seat that I wasn't able to change that outcome, because I didn't have the authority. I had asked Dick to make Bart McDade the balance sheet czar. He had the authority and knowledge because he had run fixed income for years and knew how they fixed the assets and ran the balance sheet. He could run a very specific team focused not on wouldn't it be nice to get the balance sheet down, but here's the target to meet. It was late March when started to get off the group. In the period prior, there wasn't any specific discipline.

Lerner: Was it triggered by Bear's failure?

Callan: You had the Peloton hedge fund meltdown and markets freezing up on financing. There were a host of things that were happening simultaneously. It was hard to say that you had some outside hope that things might get better. Can I say what got Dick and Joe excited? I can't. We did turn the corner and decided to set up a structure with consequences. I'm guessing why they got excited at that point.

Lerner: Do you remember a meeting at some point?

Callan: No, we sat next to each other. You just walked into each other's offices. There wasn't anything formal. The idea was constant open communication.

Lerner: Just to follow up, you talked about authority. To the outsider, you'd think that the CFO would have more authority than the head of the equities group, but you said that Bart had more authority?

Callan: It's part of why I wasn't that excited about the role. As an employee, I didn't observe it to be a powerful decision making role and it didn't turn out very different. There's a history to how all of these jobs were done and there was a sphere of influence and in the CFO role you reported the financial results but were far from creating the financial results, which was done by Joe and to some extent Dick when he decided he needed to hear about it. What asset classes, balance sheet, all came through Joe. I didn't know that ahead of time, but that was the way it was.

Lerner: Did Mr. McDade report to you?

Callan: No. He reported to Dick more than anyone and Joe. Even reporting to Joe would have been a little bit odd.

Lerner: Why?

Callan: Technically, Bart reported to Joe, but he was very powerful in the firm and with something like that, you needed Dick to ask him. That's why I went to Dick to ask McDade. It had to be from him. I recommended him, to me it was obvious; I knew it needed powerful ownership and it wasn't going to be Dick, he had stuff to do every day. It needed ownership on how the guys in equities were running their business and equities every day. It seemed obvious.

Lerner: Was there anyone else?

Callan: I didn't think of any.

Lerner: And how he was powerful?

Callan: He was appropriately influential. He ran fixed income successfully for years. He was asked to run equities and was successful. Power naturally comes with having accomplished all of that.

Lerner: And was he supportive of others at the firm?

Callan: Yeah.

Burrus: Were the goals for reduction realistic?

Callan: Yes, and they were met. They were exceeded in most cases, but undeniably were met. It was lowered to 15-20% pretty much across the board. We didn't speak to the analyst community about leverage. We spoke to them about real estate.

Burrus: When did the reductions start?

Callan: In April and May, and most was back ended, as usual, when there was the most pressure to deliver on the targets.

Lerner: In the report there was an April 2008 email about your dismay over the overall growth of the balance sheet? What was going on around then?

Callan: I don't specifically remember, certainly we were trying to go into another direction. I just wanted to come back, to clarify about when this push or action around delivering or selling off illiquid assets around, have I described this well?

Lerner: If I understand, it didn't get much traction until March. McDade became balance sheet czar, and it was successful. Over what period of time was it successful?

Callan: Just in Q2 itself. It was really just April and May.

Lerner: Was that your focus as CFO?

Callan: Getting the illiquid assets down, absolutely. To me that was the number one spot where energy should be spent. In some ways, I was the connection with the outside world. I heard feedback from investors (creditors and equity holders) and made recommendations accordingly. There were a couple of things at the top of my list: implementing some program to get illiquid asset concentrations down, giving more disclosure and being more open about our situation. Trying to give better credibility to the organization in the sharing and quality of the organization, so investors could be more confident.

Lerner: Disclosure?

Callan: Taking the cue from investors about what I wanted to know, I looked at the earning results and the firm only showed a lump result. It didn't give investors granular information, didn't give information on the asset classes, and we'd never told investors what our position was at the beginning and end of the quarter, or hedging. The biggest change was creating a whole page dedicated to identifying all of these metrics. This was a tear sheet. Page 13. This was my triumph because it was such a departure. I was very proud of it. I referred to it as "Where's Waldo." It wasn't deliberate to hide things, but like all of the things there was never a really fresh look taken in the context of earnings releases, the 10-K, and investor meetings. Investors would say that I gave them a lot more information. The facts are what they are. People will usually guess the worst case scenario. You gain credibility for being forthright. There was really a huge effort to get from here to there during my tenure in the firm. We made a ton of progress.

Lerner: Did you have any resistance?

Callan: I was given a lot of room on that. Partially because of my background, because I had been an investment banker advisor to institutions. They were ready for it. Did everybody like it? Not everybody likes change, but I didn't get a lot of pushback on it.

Lerner: Fuld and Gregory supported this?

Callan: Yeah. I made it clear from the beginning that I thought it would be important and they were supportive.

Lerner: Did you have to make changes in your office to do that?

Callan: There was one very important change that happened at the beginning of my tenure, the Controller wanted to move to IR, because the Investment Relations head was retiring. He thought IR may be fun and different, but it would have created a void in the controller's spot and he was the most important tenant. I hired Martin Kelly to work for me in that role. He raised his hand if there was going to be an opening. He had great experience. We had worked closely together. I really trusted him and had a lot of respect for him. Given that the controller's job is financial reporting, making the changes to the reporting was easier because we were both new in our roles. We were the two people responsible.

Lerner: Was it your decision to bring Mr. Kelly over?

Callan: I had various people interview him in November. I think he started in December when I started. He interviewed with Joe, Ian, and Chris to make sure he was comfortable and everybody was happy with his skill set.

Lerner: It was announced September 20th that you would be CFO –

Callan: I didn't move from my seat on the trading floor nor start getting any information until mid-October when I started getting reports and was brought in the loop.

Lerner: Around the February timeframe it was hush hush?

Callan: I was just doing my job. I didn't get any other information about the earnings call.

Lerner: Who were your direct reports as CFO?

Callan: Ed Grieb was a direct report, Paolo Tonucci, Jerry Riley who ran product control who was the liaison to the businesses, I had a head of tax, and then there were a European and Asian CFO. Seven or eight people.

Lerner: Head of Tax?

Callan: John was new in the seat. It didn't end up being something that had a lot of issues or items in that period, and we would meet a few times.

Lerner: Are there any other examples of changes you put in place regarding disclosure and transparency?

Callan: There was a lot of stuff we did to the 10-K.

Lerner: Any that stick out?

Callan: A lot of stuff about Level 3 assets – let's break it down to two components. Martin and his team made recommendations about the 10-K, and then I'd layer on top my particular areas of sensitivity based upon what I knew the world was focused on. We changed how we reported Level 3 (ways to judge timing, etc.) and we made lots of changes to the reporting of asset classes. There were voluminous amount of changes from Martin and his employee Travesary. We changed some risk reporting about VaR, to give better information. The categories were too broad, so we made smaller categories. Certainly the biggest ones were the asset classes.

Lerner: Why hadn't this been done before?

Callan: I don't really know, probably because I didn't get pushback. It seemed obvious to me at the time, but again it's obvious when you haven't been in the job for years working off the template. I saw this as an opportunity for me to add value, and it could be tremendous positive change.

Lerner: Did you work with the auditors?

Callan: Martin worked with E&Y. I may have met with them once a quarter. I did have some conversations with E&Y about either the 10-K or the Q for the quarter, and all of this was good for them. They were positive about it.

Lerner: Did you have involvement with the 2007 K?

Callan: I did, because the work on the K is done in January. I worked on it from this perspective: my ability to work with the integrity of the numbers because I wasn't involved in developing the numbers, and I did spend a lot of time on the disclosure and how it was written.

Lerner: In the vein of increased disclosure, did you have more communications than your predecessor?

Callan: This was a very structured set up. Investor meetings were set up by investor relations, so that wasn't done any differently or with greater frequency. I spoke at a Credit Suisse conference in February and at UBS in May. My understanding in the past was that Chris hadn't done the conferences, Goldfarb had. His last role was Chief Investment … and before that he was the

CIO. The frequency of investor meetings was no different, but the detail of information was more specific than in the past. We did not work off of an automatic template. It was the May UBS conference when I gave the reductions for the quarter.

Lerner: Did you have conversations with Mr. Goldfarb about what to talk about?

Callan: Not with Dave, but I did with legal. Regulation FD- prevents you from giving material non-public information in a small group, but at a Credit Suisse conference it's considered public. This is an opportunity to give more. That's why we gave the targets in the conference.

Lerner: Did you speak with Russo in legal?

Callan: Not Mr. Russo, Joe Polizato. It's a very sensitive topic of Reg FD, when you can and cannot give information. I wouldn't say I got a ton of practical feedback on that. There was confidence in my judgment on how to handle that.

Lerner: You had a conversation about Mr. Einhorn in the press, what do you remember about the conversation?

Callan: I remember having it.

Lerner: When was it?

Callan: Mid-May I think. In the teens maybe. It was really in response to his request to have a conversation. He'd already spoken a few times about Lehman in an unflattering way, and I went to Dick and Joe to say, "should I have this conversation?". It wasn't my call. They said yes, you should. I was tentative about it, because even though I was in this camp about being open, sometimes you have to recognize the impact of talking to someone with an agenda.

Lerner: Were you in favor of doing it?

Callan: No, I didn't say I wouldn't do it, but I wasn't in favor of it. I remember having the conversation and there were a bunch of specific items about the 10-K. I had Martin there with me, as the controller, and Ed Grieb from Investor Relations. Einhorn raised a bunch of points that were mostly actually misguided. He was going off into the wrong thing a few times. So we had the conversation and I said to him that I was trying to be really helpful, and I said good to have the call and I'll get back to you on Monday. And he said that he was speaking to a conference about Lehman and we had the back and forth about how he didn't say that he was going, not on the up and up. You know what happened from there.

Lerner: What was your impression from what happened there?

Callan: He had a book he was selling, and he got a lot of media attention and he took the opportunity, as you expect people to do. I was in the camp of getting talking points to say to clients as we needed to, but I didn't think we would be successful in a press strategy. Let him run with it, let's leave it and not get into a battle royale.

Lerner: Is that what you presented to Mr. Gregory and Fuld?

Callan: Yes.

And were they promoting a more aggressive strategy? All I know is that that wasn't the strategy that was implemented. That became part of the "kill the short-seller" strategy. It was always a trench warfare mentality.

Lerner: Did you aggressively say I disagree?

Callan: I would wake up in the morning and there'd be pictures of me boxing with Einhorn, and I was just trying to stay focused on my job and not get sidetracked by what I considered to be a bit of a side show. I didn't see what else was possible.

Lerner: What were the misguided points of his argument?

Callan: I'd have to go back and look, but I remember he alleged that we had a lot of CDO exposure that we hadn't reported. We had asset-backed security exposure that related to railcar receivables, etc. He referred to the securities as non-collateral, but in the footnote it said that it didn't relate to mortgages. His starting point wasn't unreasonable, but his explanation was unreasonable.

Lerner: One thing that he's talked about in that time frame was valuation issues, did he ask about that?

Callan: He did ask about a specific asset – KSK Power Plant. And again on that, Martin was there to talk about it. We went through a rigorous process with E&Y to determine a valuation for the asset, which we walked through with him and he didn't agree with it. He raised questions, but it was that outside the US there are pre-IPO valuations for companies. Part of what was relied on was a pre-valuation by Morgan Stanley on KSK. We thought it was a fair method under accounting guidance. There was also one that Lehman was part of, but there were third-parties involved. He was nit picking some of the aspects on how it was arrived at.

Lerner: Did Lehman have any sort of strategy to deal with some of the rumor mill?

Callan: I really wouldn't know, which may sound odd, but that wasn't my bag at all. I was just interested in reporting the results of the company and trying to get ourselves to a place where we could have credibility on how we present numbers and deal with investors. There was a press team that would tell me when I was meeting with press. I was just a piece, just like Dick was a piece.

Lerner: To your knowledge there was no grand strategy?

Callan: There could have been, but I wouldn't have had to be aware of the plan. I was just doing my thing.

Burrus: If we move on to capital ratios, did you have any concerns with the capital ratios at Lehman, any problems with them dropping to low, any problems?

Callan: I wouldn't say that capital ratios were a metric in terms of how we thought about the business. Unlike a commercial bank – the SEC was implementing an approach but was tweaking it – so it wasn't a way we thought about the business. The way we thought about it was from the perspective of the concentration of the assets (how liquid or illiquid), not so much the capital ratio.

Burrus: Did you have any meetings with the SEC when you were part of the CSE program, or know how often they were at the firm?

Callan: I remember a meeting. I couldn't tell you when it was, but early on (Dec/Jan) I met our SEC counterparts and we had a lunch. They got to see me and I saw them. After that, I don't remember being in a meeting with them until the March 15/16th weekend when the SEC and Fed came in together after Bear Stearns. After that, clearly they came onsite, but they weren't even in my building, they were in the building with my Treasurer. He gave them all of the day-by-day information. There was at least one more meeting down at the FRBNY that Geithner ran with Dick, Joe, Ian, and myself, in May or something, where there were members of the SEC present. My guess is that Paolo had the most contact with them and Martin may have too with onsite.

Burrus: Would you receive updates?

Callan: I would, but there weren't very many, it was more of a process of us giving them information. Not much more of an update than that that I can remember.

Burrus: Who at the SEC?

Callan: The lead was Eichner, who was not on-site. I met with him at least once, probably that first intro meeting. It was more junior staff on-site. I don't remember who was on-site.

Burrus: In the meetings you had with him, did you discuss risk tolerance?

Callan: The first meeting was just a meet and greet. It was casual, not a deep dive. The following meetings were meetings updating very clearly liquidity and capital in the wake of Bear Stearns. Ultimately, during the May meeting we talked about updates on those items and the loss for Q2. I don't remember being there.

Burrus: Did you talk about the stress testing Lehman went under?

Callan: What do you mean about that, the ones that the risk group would do?

Burrus: Yes. There was a part of the bankruptcy examiner report about Lehman failing internal stress testing and a stress testing light?

Callan: No, don't remember. Risk was an independent group. Anything to do with risk was on his watch. If it had financial consequences, I would be made aware of it, but I never heard anything about testing Bear Stearns on us or anything like that. In fairness, there was a consequence of risk appetite but other than that nothing.

Lerner: Can you talk about that?

Callan: It was a simple notion on how much tolerance did you have about losing any amount of money in any given quarter. In any given quarter what could you tolerate and feel okay if you lost an amount of money.

Lerner: Was it a percentage of earnings?

Callan: I don't know if it was a percentage, but it bore a relationship to the total earnings. At some point, I know having seen it in a board report, it was rising about at target, but they had adjusted the target.

Lerner: It was an internal document?

Callan: It was an internal concept that was not articulated to the outside world at all. I never had a conversation with investors.

Lerner: It wouldn't have been in a 10-Q?

Callan: I don't remember if there was a number in there, but a concept may have been in there.

Lerner: I think the examiner's report says there was a disclosure to the SEC that it was a hard guideline that was exceeded?

Callan: I don't know about that. I always thought it was a subjective guideline. I didn't think it was shared externally. If it was shared verbally, I wouldn't know about that.

Lerner: What about the exclusion of certain assets in stress testing, as reported in the examiner's report?

Callan: Not involved.

Burrus: At the March 2008 executive meeting you reported that Lehman Brothers was operating at near-record levels of liquidity. I'm trying to get a handle on liquidity issues, was that a concern for you as CFO?

Callan: Certainly from March 16th and on, but before that it wasn't an area of concern. It was an important area, but it wasn't an area of concern. From March, it became an area of looking at day to day and becoming comfortable with counterparties. It was always critical but moved front and center because of liquidity. Liquidity dried up, either it deteriorated or dissipated. There was a deliberate effort by Paulo to determinate out some of our liquidity. There had been some efforts since the 1998 liquidity concerns, within Long Term Capital Management. After that event, the firm reduced reliance on short term debt, concern about counterparties. It did feel like the firm was actually in pretty good shape, because there was a history of some tough lessons about liquidity that had taken place.

Burrus: The examiner's report talks about some assets that had been counted in the liquidity pool. How did that get calculated?

Callan: It wasn't the definition. It wasn't about illiquid or liquid. Rather, it was whether the asset was encumbered or unencumbered. We would get granular questions about this and break down the types of assets. The key to the definition was unencumbered.

Burrus: Did you have questions about whether the assets were unencumbered?

Callan: It came to me.

Burrus: Who calculated it?

Callan: I don't remember whether it came from Martin, Paolo, or Jerry. Possible Paolo. I was given the number of whether it was unencumbered, specifically with the holding company, which was presented and adjusted as you got closer in. It was presented as the facts. The nature of this job is that you have direct reports that you trust and delegate to, and you'd be paralyzed to dive into all topics. This seemed pretty straightforward, if they were unencumbered.

Burrus: You felt the numbers were rock solid?

Callan: I didn't have any reason to question that they weren't the right numbers.

Burrus: Did you trust the numbers from each of the three equally?

Callan: Absolutely, you couldn't be in this job if you didn't trust your direct reports. There was just too much going up and down. There were 2000 people who worked in finance alone. If I couldn't have trusted each one implicitly –

Burrus: Did you have any interaction with product control?

Callan: That was Jerry Ryan's responsibility.

Burrus: Did you have any input in the markdowns of asset values?

Callan: I wouldn't have any input, because I didn't have valuation expertise, but I was [delivered?]-- this is where the market thinks we are. There wasn't any notion of limits. Just this is what it is. We marked our assets every day, but there wasn't any ability to input into the process.

Lerner: Did you see any pressures from any seniors at Lehman?

Callan: Certainly nothing that I was aware of, and nothing that came my way. I don't mean to be hesitant – I'm trying to be careful of what I actually knew. What I actually knew isn't the whole world. Ian played a big role, in a number of topics we overlapped, but he ran with compensation, etc. He ran with things that were too many for me to take on. What was on my watch? Absolutely not.

Lerner: When I asked that question – I'm interested in the bigger picture – but did you hear that from other sources about write-downs not being taken or not taken in the full amount?

Callan: Did I hear that there was pressure about write-downs? Yeah, but it was never substantiated and I didn't get it from product control. In the way firms are rumor mills, I'd hear the vague kind of thing, but nothing that would demonstrate to me in any particular way.

Lerner: There has been a lot written about Archstone and the write-downs. Can you describe what happened there?

Callan: The process with Archstone was like any other asset, there was a validation methodology that E&Y was comfortable with – we were looking at other banks that had looked at their valuation. It was hard from my seat to exactly understand the asset. The only way to do that is to ensure that the valuation has been verified. There was only one way for me to get any comfort, which was to look at how other banks had marked it. We had marked it below where others had, and wasn't un-meaningful. This led me to know that although I can't know the valuation of this asset, I could know that this is where BofA marked the asset and we were more conservative than BofA. Obviously, over time the marks got more dramatic as the market deteriorated.

Lerner: The examiner's report discussed Mr. Geithner's remarks on air; did you see anything?

Callan: It was hard for me to come up with my own methodology to validate the remarks and rely on the E&Y marks.

Lerner: The way it's discussed is that there was some reluctance at Lehman to take write-downs because it might show that there was air in other write-downs?

Callan: That's kind of an odd theory. I don't know why it would imply that there were bigger marks. There was no reason to be uncomfortable with the marks.

Lerner: To be clear, I don't think his comment was specific to Archstone, but that the street has a view that taking write-downs means there's other air in the market. The report also says that the product control group was understaffed without proper resources in terms of models or sophistication.

Callan: I wouldn't say I had that feeling specific to product control. The overall finance group could be improved over time. We had started to make progress, through putting Martin in his seat. It wasn't a glaring issue, but I thought it could be better with more talent. When you're used to working in the front line of an organization and you're with the best producers, when you're in the center of the organization you don't see the same talent. My objective was to pull the same quality into the center. I had the ability to pull senior mangers into these roles that might -

Lerner: How would you have been able to attract that talent?

Callan: I had charisma and energy and people would say that I went from the front line and chose to be in the center of the firms. I brought people over with me from the front line to the center line.

Lerner: Was it upgrading the skill or the number of employees?

Callan: I never thought that we needed more employees, but overtime we could get more skilled people in the roles.

Lerner: How did you feel about the sophistication of the technology and models?

Callan: It wasn't my area of expertise. It would be hard to say how sophisticated or unsophisticated those models were.

Burrus: When did you first become aware of the usage of repo 105, both term and transaction?

Callan: The use of the term is hard to say. My first recollection of talking about and getting a download was sometime in March during a meeting with Martin Kelly in March 2008. It was in the context of what I asked Martin to do – was part of the best practices initiative to come up with items that he wanted to improve over time. Everything was under his watch. We had a meeting in March about what he could do, and this was one of the topics we talked about.

Lerner: What did he say?

Callan: I remember him raising it from the perspective of this is what it is, and in terms of the spectrum of accounting, is this where we want to be. He was posing it as a question of here's something we're doing and here's the information I have thus far, and whether we want to do Repo 105 transactions.

Lerner: Why would he question that?

Callan: He wasn't sure whether we were the only ones doing it. If you think about the spectrum of things that you do, you want to gauge yourself in the context of things you're doing. I asked him to go back and figure out who else may or may not be doing it, and to figure out if we were the only ones and get some more information and let's talk about it again.

Burrus: Did he come back and tell you?

Callan: This was March and things did become a little more unwieldy. It was right around March, but before Bart become Czar at the end of the month.

Lerner: What did he say about repo 105, did he mention the London legal opinion?

Callan: I don't recall, but if he had it wouldn't have meant a ton to me, because we moved assets around a lot. Having worked on financial products, we would have different opinions from different jurisdictions. It wouldn't have been a telling fact if a London legal opinion came in.

Lerner: Would it have been a telling fact that they couldn't get a US legal opinion?

Callan: Yes, very telling.

Lerner: Did he describe the nature of the transactions?

Callan: I think so. It was easy to describe. My feeling was that he'd done some preliminary work, but was really unsure, and was going to talk to E&Y and figure out who else was using it.

Lerner: Did he talk about treating a repo transaction as a sale?

Callan: Well that's what it was – he told me it was accounted for as a sale.

Lerner: Did that cause you any concern?

Callan: No, I worked on a number of transactions that accounted for as a sale under FAS 140. Accounting is a very rules-based system and you have to comply in a very obvious way with the rules. Tax tends to be more policy and concept in nature. My understanding was that there wasn't any question that it was an accounting suggestion. The point was that lots of transactions might be accepted, but where do you want to be in terms of what you want to do.

Lerner: Further out of the curve on the transaction?

Callan: The whole notion of the transaction itself is this one that you thought was very strict if you did it right, or would you rather be doing things more conservatively.   That was my impression, not that there was any question about the acceptability but in best practices, are we unique in doing it.

Lerner: It strikes me that you were getting close to the brink of doing something that may not be acceptable?

Callan: Not at all. It is as conservative as we want to be. If you're ever the one to be doing anything, you don't want to be the only guy using a certain methodology. In terms of best practices, you don't want to be on the brink of doing anything. I didn't have any interest in being an outlier on any of the issues. He never said that to me, it was my understanding of why we were having a conversation. The reason was because he thought that there may be a chance that we were the only firm using it and it may make you pause and think about what you want to do.

Lerner: Did he raise the volume on how $50 million was running through repo 105 at the time?

Callan: My recollection at the time was that it was something like $20 million.

Lerner: According to the examiner's report that at Q12008 it was $48 million?

Callan: That sounds right in retrospect, but I couldn't have told you any of that at the time.

Lerner: Did Mr. Kelly raise that to you?

Callan: We may have talked about a volume but it was $20s.

Snell: There are graphs in the examiner's report.

Callan: I don't remember talking about it from quarter end.

Lerner: Did he say anything about it spiking at quarter's end?

Callan: No

Lerner: Did you know that it was spiking?

Callan: No

Lerner: Did he mention anything about a reputational risk of repo 105?

Callan: He made some reference to either perception or reputational. Where do we stand with our peer group in terms of these transactions, and if we're an outlier, what would that mean. It was embedded in this whole topic. He was raising it in the context of how do we feel about doing this. It was very circular because we didn't know the answer of whether we were doing it.

Lerner: It seems that being the only ones doing it, and reputational risk, are different concepts?

Callan: Not to me. The reputational risk would come from the fact that you were alone in using this methodology.

Lerner: Is it possible to have reputational risk if you're one out of many?

Callan: Sure. This was a five minute conversation, but on a very cursory level. It's your shorthand of whether there is risk associated based on who else is doing this. On this particular thing, in and of itself, no one was telling me that it was wrong, but the suggestion that we were the only one doing it and whether to continue doing it.

Lerner: There's a difference between knowing that you're doing it and risk. What risk did you or Mr. Kelly see?

Callan: I can't be sure what was going on in his head, but the way I was thinking about it is that the way you do things – you like to do things to be in best practices. I was trying to be best in class of the things we could control from our office. To be best in class, you do things in the most thorough and conservative way possible. All I heard was that it's okay from a gap perspective. The presumption was that it was reasonable. The only way to spend time on it was that we may be the only one doing it. Maybe there's something I'm not appreciating.

Lerner: It still seems to me that there was an underlying risk that you were concerned about?

Callan: Based on what, that I was asking him to do homework? He raised the issue so he had to have some level of concern about it.

Lawyer: It seems to me that your perception is that you don't fully accept that being an outlier could be the genesis of reputational risk?

Callan: The only thing I heard that made me think that it was something to spend time on it, was that we were the only ones doing it. In fairness, this was a conversation that involved other topics, like system and talent upgrades, and this wasn't at the front end of the discussion. The contents as presented weren't "I have a concern about this," it was an "FYI this is what we're doing and here are the facts on it." He thought we were the only ones doing it.

Lerner: If I understood you correctly, you didn't hear follow-up, but you didn't look into other firms?

Callan: That's his job.

Lerner: Did that become an issue that just didn't get developed?

Callan: It happened because we were in a full-scale financial crisis. This had been a wish list of topics of things we may do overtime in terms of a Controller job, and when we can we're going to do these things. That kind of initiative wasn't a front burner initiative.

Lerner: If he had said we're doing $50 million a quarter, would you have stopped?

Lawyer: It's tough to answer those questions.

Lerner: I'm just trying to get at what the examiner said.

Callan: The examiner's report, as I understand it, was about disclosure. Martin ran disclosure, but to me, if you thought it was material risk, a particular item, he would say to disclose this.

Lerner: You relied on him about disclosure?

Callan: He ran through all of the nuts and bolts and I would overlay the big picture investor piece. It was never suggested as a disclosure item, which was in keeping with the way I understood the issue.

Lerner: You said that there may have been other things done at quarter's end that you wouldn't want others to know you did?

Callan: I was referring to the Fed report about banks increasing and decreasing things over time. I didn't mean to imply that you wouldn't want people to know about that.

Lerner: From a policy note, is that an area of concern?

Callan: I don't know. For who?

Lerner: Investment firms, etc.

Callan: I don' really have a point of view on that. I took it as this is how the industry operates.

Burrus: In regards to the 105, the whistleblower letter from Matthew Lee. Who brought that to your attention?

Callan: I think a copy was left on my chair. It was a few weeks before I resigned.

Burrus: Did you read through the letter?

Callan: Yes.

Burrus: Did you have discussions about the letter?

Callan: We had a meeting with our general counsel and Joe.

Burrus: Mr. Lee was in your shop?

Callan: He worked under Martin.

Burrus: When you saw those topics was it concerning to you?

Callan: 36CFR1256.56: Privacy [redacted] It was taken off my plate. When I resigned on June 12, I'm not sure how things progressed, other than it was being diligently addressed by the audit team.

Burrus: Are you aware of any other off-balance sheets Lehman used besides Repo 105?

Callan: Nothing, I didn't know anything specific. There are specific vehicles that could be used. There were things like that. Nothing very obvious.

Lerner: On the Matthew Lee situation, what was the history between Mr. Lee and Mr. Goldfarb?

Callan: Goldfarb hired him when he first became CFO and felt loyalty to him. 36CFR1256.56: Privacy [redacted] It was easier to go to Martin on that. It was out of his chain of command. I told Martin to tell Dave to hire him if he loved him. I didn't know the guy, he worked for Martin.

Lerner: Was there anything suspicious between Goldfarb and Lee?

Callan: No, he was loyal and had the people who were in the seats with him. He felt some responsibility for that. It was hard to see, because a lot of people who were around for a long time were leaving.

-BREAK-

Burrus: What is your knowledge about the derivatives, the Lehman strategy with OTC derivatives?

Callan: None, I never worked with that part of the firm, I don't even know what you mean about the strategy.

Burrus: Let's switch topics to compensation.

Callan: I never got paid for being CFO.

Burrus: Did you have any input on the people who worked for you on compensation?

Callan: I never went through a compensation cycle. I saw numbers in December, so I had input into my hedge fund group, but not the new group. The whole comp process was really run by Ian. Joe in the end was calling the shots, but Ian was getting all of the information together on the comp.

Lerner: You really weren't compensated in 2008?

Callan: I may have been paid $100,000 for being CFO. I decided to resign so I lost all of my unvested stock and I didn't get paid. I made a decision about making a change.

Lerner: How did your resignation come about, it seems like a very dramatic event?

Callan: It was really as the second quarter was materializing and we were going to have a big loss, I had a lot of concerns about that and the responses in the broader market. We had started a confidential over-the-wall capital raise five days before the public capital raise. We had 20 investors and had to tell each one of them about the quarter. There's not a more depressing thing than telling all of our biggest investors about what had happened, and it was just challenging and despite what I could actually control, the outside world assumed that I could control the performance of the company. As I started having those conversations, I knew that it was absolutely in line with my worst concerns. People would lose confidence in the company. It wasn't as real to anybody else because I would do them by myself, 45 minute conference calls all day and night. This was part of the job. I did say to investors that they could speak to Dick, and he got a few conversations. He didn't like doing them. It was in my job description to have these conversations. There were a couple of specific conversations about the real estate stuff, held by Mark Walsh. But it became clear that this would be disastrous in response, and I said look, no one is more closely aligned with the performance of the firm and I'm willing to resign. I may have had this conversation on Wednesday the 4th. By Friday the 6th I went to Dick and said how bad it was. On the 9th, I talked about it again after the conference call and on the morning of the 10th at the executive committee meeting, a voice was heard that heads needed to roll. I heard that meant getting Joe out of his seat, but again I think there's an email I sent to Dick saying that I get it, things need to happen and I'm offering to resign. The next day Joe came to me and said we're going to do this together.

Lerner: Was it your understanding he had discussed this with Dick?

Callan: Yes, I talked with Dick about it and we talked to the exec committee.

Lerner: How did the investor call go on the 9th?

Callan: Terribly. There was a lot of bad information and at least we could show that we had turned the corner on our philosophy, but in terms of shaking people's inner confidence, I said that I don't think I can represent a credible spokesperson at this point because I'm associated with the shaken.

Lerner: When you were talking to Mr. Fuld on Wednesday, did you think you would survive it?

Callan: I did, it was a surprise even though I offered it and it was the right thing to do, selfishly it was upsetting.

Lerner: Did you feel like they had misrepresented in the prior conversations that you'd be okay?

Callan: No, I think Dick changed his mind, because in the aftermath you're entitled to change your mind. My only gripe is how they presented it that I got canned when I offered to resign. It stayed with me for a long time, that's why I never went back and why I couldn't stay. It was a huge point reputationally. And it wasn't acknowledged publically.

Lerner: Why do you think they did that?

Callan: I have an opinion that most of what happened was in the interest of making Dick look good and it made him stronger to fire me.

Lerner: His strength, to save the reputation of the firm on the Street?

Callan: He was the firm, and it's hard to distinguish him and the firm.

Lerner: Did they feel they needed to send this strong signal to Wall Street that we're taking action?

Callan: Yes, that's my interpretation. When I told Dick he seemed surprised that I thought it looked like I got fired. He didn't run the press machine, so I can't say whose decision it was.

Lerner: How did Mr. Gregory's termination come about?

Callan: It was clear to me that there was a lot of agitation about him staying in the role. And at the executive committee Skip was talking about Joe when he said that we need senior management change. I've only heard afterwards about the clandestine meeting of the bankers with Joe. He made all the big decisions and ran the firm. He was primarily the point person on the mortgage business forever, and he was the person to be accountable. I think it was heartbreaking to Dick to fire Joe. I didn't know it to be a package deal, because I had offered to resign. In the end, in retrospect it was a package deal because Joe didn't have a reputation, but internally it was a big deal because Joe called the shots. Externally, people knew me.

Lerner: There's been a lot written up about how Mr. Gregory was terminated. There's an account of McDade walking in and telling Dick that Joe has to go?

Callan: All I know is what happened at the executive committee and Joe saying that we're doing it together. I had to do the pre-earnings call, and had to do another earnings call. I was sitting in a room writing an earnings transcript. I couldn't even see people walking into Dick's office because I was off in a conference room.

Lerner: Was anyone out to get you?

Callan: That's not the way I think; I hope not.

Lerner: Was anyone out to get Joe? I think he was a polarizing individual.

Callan: Probably a little more extreme than some people.

Lerner: Polarizing?

Callan: Either you were a fan or not a fan and he was either a fan of yours or not. There was no gray.

Lerner: How was he as a manger?

Callan: For me, very good. He would give direction, access, and a lot of running room.

Lerner: Did you like him and appreciate working under him?

Callan: Yes, I wouldn't have taken the job if I didn't think I would get along with him and Dick.

Lerner: Do you keep in touch with him?

Callan: No.

Lerner: Did you talk to McDade during this period?

Callan: During my resignation time, no. It wasn't natural for me to go talk to him. I wasn't a political person who was up on gossip and who was rising and falling. I was having a hard enough time commanding my job. Was I aware that some people did or didn't like Joe? Of course. Was I a person to come to and say we have to get rid of Joe? No.

[Per 4/28/2010 Email from Callan's counsel, "Upon reflection following your interview of her this past Monday, Erin would like to clarify some details in her account of the sequence of events leading up to her departure as Lehman's CFO. She believes she first raised the issue of resigning as CFO with Dick Fuld following the meeting of the Executive Committee that occurred on the morning of Tuesday, June 10, 2008, at which (as Erin told you in the interview) the issue of accountability was discussed. She then raised the issue, both in person and by email, with Fuld later that day. Erin reiterated her offer to resign as CFO in a meeting with Fuld the following day, June 11, 2008. Although Fuld initially refused to accept the offer, later on June 11 Joe

Gregory came into Erin's office and told her that the two of them were "going to do this together."]

Burrus: What do you know about Lehman trying to obtain bank holding status?

Callan: That was really after my time, I never walked in the door after June 12th. There were a couple of meetings with Rodge Cohen from Sullivan Cromwell, who's a well-known lawyer. He came in a couple of times to talk about that possibility and trying to present to Paulson and Geithner about that status. When I left that was still in the process.

Burrus: You touched earlier about capital raises, how many of those did you undertake?

Callan: I'll be strict about the definition of capital because there was obviously a lot of long-term debt raising, because I was getting info from people in the debt markets that they could shut down. In February we got a good deal at a great price. There were two significant capital raises, the April 1st $34 billion where our stock had performed reasonably well in the aftermath of our earnings announcement and it felt like we may be okay. But, by the second week our stock was drifting down bit by bit. I went to Dick and Joe and said that we needed to raise capital and executed on convertible. It was the first big trade in capital since the firm went public. The second was done after the Q2 announcements. It closed on June 9th. We rounded up straight common stock and mandatory convertible stock, $6 or $7 billion. That was connected with replenishing the loss. I think the February was $1.7 billion at a 7.25 coupon.

Burrus: In accordance with Sarbanes-Oxley, you had to sign off on the financial statements. What was the process for the certification?

Callan: There's an extremely elaborate process with hundreds of people. It runs from the trenches of the business and all of the way up. Each manager looks down on their chain, and would culminate at the end of the quarter with the top people on the re-certification and sub-certification process. This would come from every business division head. There was a roundtable with 50 people and then those people have people sub-certifying. There's not an independent way for Dick or I to say whether the mark was appropriate on the equity trade. The only way you can do that with some sense of confidence was through business certification.

Burrus: So the business heads would certify to Martin?

Callan: No, to Dick and me. I went through it twice, and was clearly an elaborate process that had been in place for a while.

Burrus: Were you part of the process in the 10-K?

Callan: Yes, in that I signed because I was involved in the K, but Chris sub-certified to me.

Burrus: Was there some process that Fuld had in addition to you to certify?

Callan: No, it was all in one fell swoop.

Burrus: Would there have been an opportunity for others to raise issues?

Callan: Absolutely. There were 50 people in the room and there were people who had sub-certified. These were the fifty most senior people in the business. It was never suggested to me that someone had not certified. I thought it was a process. Simpson Thacher and E&Y were there. Repo never came up.

Burrus: Why do you think Lehman brothers failed?

Callan: I was shocked by it, which tells you I don't really understand it. It would never have occurred to me that it would have been the outcome.

Lerner: Even after two big quarter losses?

Callan: Yeah, we saw others having multiple quarters of losses. Merrill had three or four quarters, Morgan Stanley had two or three. You can survive losses indefinitely if you have liquidity. The losses did not mean that the firm would be bankrupt. I don't know the whole chain of events.

Lerner: Was one of the factors the third quarter loss?

Callan: That would be relevant, but it didn't definitely mean that bankruptcy would occur.

Lerner: Do you keep in touch with anyone?

Callan: Nobody.

Lerner: In your mind, what were the causes of the financial crisis?

Callan: I don't have any great insight other than what became apparent was the contagion effect, and that's what was underestimated. What initially appeared as a problem with mortgages and was thought to be contained within mortgages, exasperated the problem. Being uncorrelated was a real thing – a notion – and in the end, when you truly have a market that suffered a crisis around an important singular asset class, the other classes become in-crisis pretty quickly. From the seat I sat in, what became apparent was how highly correlated the asset classes were. All that a good appreciation would do was that people would have gotten out of the markets faster. You would have gotten to the same place with people wanting to get out and people not wanting to go along at the time. There was not a lot of cash and leverage. Leverage, as the simplest observation was the use of leverage, which was still a pretty nascent concept. Just how far the market had moved toward leverage buyers.

Lerner: It's interesting because you talked about leverage separate from illiquid assets.

Callan: The problem is that people were using fairly high amounts of leverage on classes that became illiquid. At the time they were liquid. That's about as much as I can say about it. You just didn't have the natural buyers.

Lerner: I just wanted to explore what you saw in terms of the relationship between Joe and Dick and how it worked in terms of not running the firm?

Callan: They got along great. I never really saw any schisms. Joe was responsible for running the firm day to day. Dick was the CEO and Chairman, and not the operational guy. I never had a sense that Joe kept things from Dick. I'm sure things were filtered by how much information you could give a person on any specific day. To me it looked like a great working relationship. Dick was the CEO big picture guy, and Joe was truly the COO, stayed in the building and made decisions.

Lerner: And you thought it worked for Lehman?

Callan: I thought it did. I don't see any fatal flaw in that business. The relationship itself and how it functioned seemed fine.

Lerner: Is there anything that you'd like clarify?

Callan: I don't think so.

Lerner: Is there anything we didn't cover that we should know about or be aware of?

Callan: No. Honestly, I guess the only thing I could say was that Lehman was not particularly unique. The timing of certain asset classes and what that meant to the company; and if they had a CDO exposure and not repo they may have survived. But in the end, they were not unique. It's unfortunate that their asset class timing was late.

Lerner: Was the commercial real estate exposure at Lehman more vulnerable than at other firms?

Callan: I think other firms were vulnerable but they collapsed earlier and the firms could go get capital. In a weird way it would be better to take a loss at the front end like Morgan Stanley or Merrill. I don't think their circumstances were really unique.

Lerner: Was commercial real estate worse?

Callan: No, it just came later in the process.

Lerner: Thank you.