From: Jamie.McAndrews@ny.frb.org
To: Patrick Parkinson; Jeff Stehm
Subject: Fw: Default Management Group 9 Sep 2008.doc
Date: 09/11/2008 02:06 PM
Attachments: Default Management Group Sep 2008.doc

For the meeting you are listening in on.

Jamie

Sent from my BlackBerry Wireless Handheld (www.BlackBerry.net)

----- Original Message -----
From: Jamie McAndrews
Sent: 09/11/2008 02:01 PM EDT
To: Tobias Adrian
Cc: Beverly Hirtle; Michael Schussler
Subject: Re: Default Management Group 9 Sep 2008.doc

Some edits:

(See attached file: Default Management Group Sep 2008.doc)

Tobias Adrian/NY/FRS
09/11/2008 01:40 PM

To
Jamie McAndrews/NY/FRS@FRS

cc

Subject
Default Management Group 9 Sep 2008.doc

[attachment "Default Management Group 9 Sep 2008.doc" deleted by Jamie McAndrews/NY/FRS]

- Default Management Group Sep 2008.doc

Lehman Default Management Group

Purpose:
Convene a representative group of Lehman counterparties and creditors to make plans in the event of a bankruptcy filing by Lehman.

Under the auspices of the FRBNY, the group would initially consist of trading partners who trade contracts that are resolved outside the bankruptcy process, such as derivatives, swaps, QFCs, repos, commodities futures, etc. One set of firms that meet this definition would be all member firms of the CRMPG. The key is that firms conduct a "critical mass" of trades with Lehman, so that the close out of other trades would not confer large external costs on the market.

The purpose of the group is to reach a public agreement by the members of the group to hold off on fully exercising their contractual rights to close out their trades with the defaulting counterparty. Specific potential agreements could include an agreement to establish a process to net down all exposures versus the defaulting counterparty and an agreement to use a common valuation for marking positions after the bankruptcy filing.

Idea: There are three possibilities for the weekend: 1) single institution taking over, 2) consortium taking over, 3) bankruptcy.
<u>Unless we have credible bankruptcy plan our negotiating position for limiting the subsidy in the liquidation consortium option will be weak.</u> Consequently, planning for a bankruptcy will reduce some of the expected costs of bankruptcy and externalities imposed on the financial system as a whole, and make it a more viable alternative.

Timing: Contingent on the anticipated bankruptcy filing by Lehman, on Friday evening, after the markets have closed, issue invitations to the chief risk officers of the member firms. The meeting would convene at 9:00 a.m. on Saturday at the FRBNY, and continue through to Sunday evening.

Membership: Because the focus is primarily on the trading partners of Lehman, the membership will be broadly representative of the major financial counterparties of Lehman, including derivatives, futures, swaps, commodities, and repo counterparties. In addition, major regulators, both domestic and foreign, will be informed of the activity of the group.

A second, larger, group could be convened on the day of the bankruptcy, which would consist of all major creditors of the defaulting party.

Outcome: A public statement of the framework to which the members would have agreed. To be issued on Sunday evening.

Antitrust concerns: There is a concern that the group could engage in illegal price setting or other restraints of trade. To prevent this, the group should be open and it should rely on legal advice to avoid such agreements.

Activities of the group: During the weekend, the group would review their options for agreement on netting offsetting agreements, reaching common valuations for contracts post-bankruptcy, and achieving a framework for addressing all the issues that will arise after the bankruptcy filing. The Fed's role would be to be a neutral party that could assist the group in communicating to the public, and provide "cover" for the membership of the group (many excluded parties will feel that they are unfairly excluded).

Pros and Cons:
-Antitrust concerns; could include an attorney from the DOJ antitrust division
-Improved the Fed bargaining position for a resolution outside of bankruptcy
-Improved outcomes if bankruptcy were to occur.