Testimony of

Harvey R. Miller[1]

before the

Financial Crisis Inquiry Commission

for hearing on

Examining The Causes Of The Current Financial And Economic Crisis Of the United States And Of The Collapse Of Lehman Brothers

September 1, 2010

I greatly appreciate the opportunity to participate in this hearing and in assisting the Financial Crisis Inquiry Commission ("Commission") in its investigation of the financial crisis which erupted in September of 2008 and was highlighted by the financial collapse of Lehman Brothers Holdings Inc. ("LBHI") and its affiliates (collectively, "Lehman"). The demise of Lehman precipitated consequences for the financial system and the worldwide economy that were largely unanticipated.

I am a practicing attorney and a senior member of the international law firm of Weil, Gotshal & Manges LLP ("Weil") that maintains its principal office in New York, New York. During my professional career, I have represented debtors, secured and unsecured creditors, trustees in bankruptcy, creditors' committees, equity interest holders, asset purchasers, and I have served as a trustee and as an attorney in cases under the Securities Investor Protection

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[1] Senior Partner, Weil, Gotshal & Manges LLP, New York, New York. The views expressed in this testimony are expressed solely on behalf of myself and not on behalf of any other person or entity.

Act of 1970 (15 U.S.C. 78aaa et seq.).[2] Currently, I am the lead bankruptcy attorney for Lehman and also for Motors Liquidation Company, formerly known as General Motors Corporation, in the prosecution of their respective bankruptcy cases under chapter 11 of title 11 of the United States Code ("Bankruptcy Code") that are pending in the United States Bankruptcy Court for the Southern District of New York (Case Nos. 08-13555 (JMP) & 09-50026 (REG)).

I am currently an Adjunct Professor of Law at the New York University School of Law, where I have taught a seminar on chapter 11 bankruptcy and reorganization law since 1975. I also am an Adjunct Lecturer in Law at Columbia University School of Law, where I have taught a course on Corporate Reorganization and Bankruptcy Law for the past ten years. I have also lectured and written extensively on the subject of bankruptcy and reorganization.

It is my understanding that the Commission is seeking information as to (i) the circumstances surrounding the commencement of the Lehman chapter 11 bankruptcy case on September 15, 2008, and (ii) whether the failure by the government or other parties to support or assist Lehman was ill-advised and may have been a major factor in the economically devastating events that followed the commencement of the chapter 11 bankruptcy case. Those consequences included a severe loss of public confidence in the financial markets and almost caused an implosion of the financial system. In that context, the Commission has asked the penultimate question, "was Lehman Too Big To Fail?"

Lehman's Retention of Weil

Weil's representation of Lehman extended back to 1984. During the course of this relationship, Weil was never engaged to or acted as general counsel for Lehman, or was

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[2] Since approximately 1973, I have been a conferee and member of the National Bankruptcy Conference and I also am a fellow of the American College of Bankruptcy.

involved in the issuance of securities by LBHI. Rather, Weil represented Lehman in connection, generally, with independent specific transactions and matters as requested. Weil provided legal services on behalf of Lehman that involved almost all legal disciplines, including but not limited to services relating to banking, finance, corporate governance, securities, mergers and acquisitions, taxes, real estate and litigation. As a result, Weil became familiar with many aspects of Lehman's various business activities and to a limited degree, Lehman's financial affairs and capital structure. Likewise, Lehman became familiar with the broad range of legal services provided by Weil, including its widely recognized business finance & restructuring expertise. As a result, during the week of September 8, 2008, as the economy continued on a downward spiral and Lehman was confronting a potentially fatal liquidity crisis, it turned to Weil for assistance.

The first communication to Weil as to possible contingency planning was during the middle of the week of September 8, 2008. Steven Berkenfeld, the then head of Lehman's Legal, Compliance and Audit Division, called Steven J. Dannhauser, Weil's Chairman, to engage Weil on a confidential basis to assist Lehman in contingency planning if Lehman was unable to resolve its evolving liquidity crisis. Soon after that call, Mr. Dannhauser alerted me to the engagement and on Thursday, September 11, 2008, I began to assemble a small working group to perform preliminary organizational work gathering information as to Lehman's financial affairs. The Weil working group had no contact with Lehman and during that period no information was furnished by Lehman. The focus of the Weil team was on publicly available information regarding Lehman. Weil also was admonished that the engagement should be treated as highly confidential.

Discussions with Government Regulators Regarding a Potential Lehman Bankruptcy

During the late afternoon of Friday, September 12, 2008, I received a telephone call from Thomas A. Russo, then Lehman's Chief Legal Officer, requesting attendance at a meeting at the Lehman headquarters that was about to start with representatives of the Federal Reserve Bank of New York ("NY Fed"). It was my understanding that the meeting had been requested by the NY Fed to discuss Lehman's liquidity. By the time that I arrived at Lehman with my partner, Richard P. Krasnow, the meeting had begun. Approximately four or five representatives of the NY Fed were in attendance. Mr. Russo initially presided over the meeting. A number of representatives of Lehman's financial staff were also in attendance, including Ian Lowitt, then Lehman's Chief Financial Officer and Co-Chief Administrative Officer. Mr. Lowitt and his associates attempted to provide the meeting with a report as to Lehman's liquidity. The essence of Mr. Lowitt's presentation was that Lehman would be unable to produce a definitive conclusion as to its liquidity until late that evening or early Saturday morning because of the complex calculations that would have to be made after the close of financial markets and the receipt of financial information from Lehman's global offices. In addition, Mr. Lowitt noted that the calculations would have to take into account the effect of the increasing demands for collateral security made by Lehman's clearing banks and, particularly, JPMorgan Chase. Before the end of the meeting, Mr. Russo had to leave to attend another meeting concerning a potential transaction that might alleviate Lehman's financial needs.

At the September 12, 2008 meeting, there was no discussion as to the probability of Lehman seeking or being subject to the commencement of a bankruptcy case. No urgency was expressed as to the need to prepare any pleadings or other documents necessary to a

bankruptcy filing. There were very brief comments made that intensive negotiations were in progress as to a potential sale or merger of Lehman with another financial institution.

Later, during the evening of September 12, 2008, I received a telephone call from James L. Bromley, a Partner in the New York law firm of Cleary Gottlieb Steen & Hamilton LLP, which was acting as attorneys for the NY Fed. Mr. Bromley inquired as to what preparations were being made to deal with the potential bankruptcy contingency. I explained to Mr. Bromley that during the meeting earlier that day at Lehman's headquarters, neither NY Fed representatives nor the Lehman representatives indicated any urgency to accelerate preparation for a potential bankruptcy contingency. I asked Mr. Bromley if anything had changed and he suggested that we should meet Saturday morning, September 13, 2008. During that conversation, I told Mr. Bromley that gathering the necessary information from Lehman was very difficult because almost all of the senior Lehman personnel were consumed in the pending sale or merger negotiations and were not accessible by the Weil team.

During the morning of Saturday, September 13, 2008, Mr. Bromley and four or five representatives of NY Fed met with me and other members of the Weil team at Weil's office. At that meeting, I again reiterated that progress in preparing for the bankruptcy contingency was very slow because of the lack of access to responsible Lehman personnel and resulting inability to obtain necessary financial information. The representatives from the NY Fed and Mr. Bromley appeared more concerned as to the need for accelerating the preparation of pleadings necessary for the bankruptcy contingency. However, they were not specific as to why or whether the situation had changed in any material manner. The meeting lasted from one to two hours. After the meeting, the Weil team, using publicly available information, attempted to prepare the necessary pleadings to be used if the bankruptcy contingency arose. During the

course of that day, it appeared that the bankruptcy contingency remained a remote possibility and that a transaction involving a merger or sale with Barclays or Bank of America appeared promising.

During the morning of Sunday, September 14, 2008, there were many telephone exchanges and conferences with Lehman representatives. It appeared from those communications that Bank of America had withdrawn from any sale or merger negotiations and that there were reservations as to the probability of any transaction with Barclays.

During that Sunday afternoon, the situation began to appear more tenuous. I was advised that a request was made by the NY Fed for Lehman representatives to attend a meeting at the NY Fed in lower Manhattan. The meeting took place in a large conference room at the NY Fed. Lehman was represented by Bart McDade, Lehman's then President and Chief Operating Officer, Alex Kirk, Lehman's then Global Head of High Yield and Leveraged Loans, and an additional Lehman officer, as well as representatives from Weil, including me, Stephen J. Dannhauser, Thomas A. Roberts, Co-Chair of Weil's Corporate Department, and Lori R. Fife, a senior partner from Weil's Business, Finance & Restructuring Department. Representatives of the NY Fed, the United States Securities and Exchange Commission ("SEC"), and, I believe, the Securities Investor Protection Corporation ("SIPC") were in attendance. There were approximately 25 or more persons facing Lehman's representatives across the conference room table[3]. The meeting had started before the Weil team arrived. The discussion at the meeting was led by Thomas C. Baxter, Jr., the General Counsel of the NY Fed, an unidentified senior staff member of the NY Fed, and Mark A. Walker, the Managing Partner of Cleary Gottlieb Steen &

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[3] To the best of my knowledge, the government attendees were not identified.

Hamilton LLP. While the primary spokesman for the NY Fed was Mr. Baxter, comments were made by others present.

In substance, the Lehman representatives were advised that a transaction with Barclays was not going to occur and, further, that there would be no federal assistance provided to save or support Lehman. Despite requests for elucidation as to the basis of the decision, Lehman's representatives were instructed that there would be no further information provided as to the basis of the decision to refrain from providing Lehman with financial support or other assistance.

Lehman's representatives emphasized that assistance from the NY Fed was necessary for Lehman to open for business the following Monday, September 15, 2008. Notwithstanding, it was clear that governmental assistance was not to be provided, except as to Lehman's primary broker/dealer subsidiaries, as discussed below. Inquiries were made by Lehman's representatives as to whether there had been a realistic and comprehensive evaluation as to the potential consequences of Lehman's failure. The responses from the NY Fed and others was not illuminating. It appeared that the definitive decision not to assist or support Lehman had been made before the meeting with Lehman had commenced and the government representatives were not prepared to discuss the rationale underlying the decision or their evaluation of the potential consequences.

The only discussion of any assistance related to Lehman Brothers Inc. ("LBI"), Lehman's New York based primary broker-dealer subsidiary. It was acknowledged that LBI, as a "stock broker," did not qualify as a "debtor" under the Bankruptcy Code for the purposes of chapter 11. The discussion as to LBI focused on its ability to continue to operate for a limited period to facilitate transfers of customer accounts. The NY Fed indicated that it would continue

to provide overnight repurchase loan transactions for LBI through the Primary Dealer Credit Facility that had been earlier established, provided that LBI pledged collateral security consistent with the requirements established by the NY Fed, albeit that in the existing circumstances, those requirements would be relaxed to some extent.

Throughout the meeting, Lehman's representatives continued to describe the gravity of Lehman's situation, arguing that a global financial crisis would result from the failure of Lehman that could best be described as a financial "Armageddon." After listening to comments from Lehman and Weil, Mr. Baxter stated that the government representatives would caucus to consider Lehman's comments. The government representatives then left the conference room for approximately one hour. When they returned, Mr. Baxter reported that after consideration of all of the contentions made on behalf of Lehman, the decision not to support Lehman had been reaffirmed. Accordingly, he stated that the only alternative was that Lehman had to fail. Mr. Baxter then directed that the Lehman and Weil teams should promptly return to Lehman's headquarters and arrange for a meeting of Lehman's Board of Directors to be convened for the purpose of adopting a resolution authorizing and directing LBHI to commence a bankruptcy case before 12:00 midnight of that day.

At that juncture the Lehman representatives reiterated that allowing Lehman to fail and commence a bankruptcy case would have dire consequences. The Lehman representatives urged the need for more information as to the rationale so they might adequately explain the position of the government to Lehman's Board of Directors. The response was that the NY Fed and others was that there existed no obligation or duty to provide such information or to substantiate the basis for the decision not to aid or support Lehman. In response to questions of whether or how the NY Fed evaluated the risks and consequences of Lehman's

failure, the response was that the government had evaluated the attendant risks and intended to take appropriate action to offset any potential consequences and thereby calm any negative response of the financial markets.

The Lehman representatives were informed that press releases had been prepared that would be issued after the announcement of Lehman's bankruptcy which the government believed would have the desired effect of calming the financial markets and public investors. The direction to return to the Lehman headquarters was repeated. The Lehman and Weil teams were encouraged to promptly leave the premises and did so.

Lehman's Board of Directors previously had been convened for a meeting at 1:30 P.M. that day at Lehman's headquarters to approve the potential transaction with Barclays. As a result, Lehman's Board of Directors was present at Lehman's headquarters when Messrs. McDade and Kirk, and the Weil team, returned form the meeting at the New York Fed. Messrs. McDade and Kirk, and the Weil team, reported to the Board of Directors the events that had occurred during the earlier meeting with the government representatives.

The report was followed by an active discussion among Lehman's Directors. The discussion was interrupted when Richard Fuld, then Lehman's Chairman and Chief Executive Officer, was advised that a telephone call had been received from Christopher Cox, the Chairman of the SEC, requesting the opportunity to address the Board of Directors. The Board of Directors concluded that in the circumstances it would be appropriate to hear from Mr. Cox. The telephone conference was opened and Mr. Cox introduced himself and Mr. Baxter. They then addressed the Directors.

In substance, Messrs. Cox and Baxter stated that it was in the best interests of the financial system and the United States economy for Lehman's Board of Directors to pass a

resolution approving the commencement of a bankruptcy case prior to 12:00 midnight of that day. Several Directors asked Messrs. Cox and Baxter whether they, on behalf of the NY Fed and the SEC, were directing the Board of Directors to adopt a bankruptcy resolution. In response, Mr. Cox hesitated, and Mr. Baxter suggested they hold an offline caucus. After five or ten minutes, Messrs. Cox and Baxter rejoined the conference call with the Directors.

Mr. Cox stated that he and Mr. Baxter were not issuing a direction to the Lehman Board of Directors to pass a resolution authorizing the commencement of a bankruptcy case. Rather, he indicated that the decision was for Lehman's Directors to make in the exercise of their business judgment and discretion. Such response notwithstanding, Lehman's Directors persisted in asking for a clear and definitive answer to the question of whether the NY Fed and SEC were directing the passage of a bankruptcy resolution. These questions precipitated another caucus that extended for another five to ten minutes. When Messrs. Cox and Baxter rejoined the conference call, they reiterated that the decision of whether to adopt a bankruptcy resolution was a decision for Lehman's Board of Directors to make and, further, that neither the SEC nor the NY Fed was directing the adoption of such a resolution. However, Mr. Cox stated that he believed that the preferences of the NY Fed and the SEC had been made unequivocally clear to Messrs. McDade, Kirk and others at the meeting that had been held earlier that day at the NY Fed.

After the conference call with Messrs. Cox and Baxter ended, Lehman's Board of Directors reviewed the facts and circumstances in light of the liquidity crisis confronting Lehman. The Board concluded that the commencement of a bankruptcy case by or against Lehman was inevitable. The Board then determined and exercised its judgment to adopt a resolution authorizing the commencement of a chapter 11 bankruptcy case by LBHI.

Pursuant to the Board's resolution, and in an atmosphere of extreme turmoil, anxiety and a level of chaos, a chapter 11 bankruptcy petition was cobbled together. At approximately 2:00 a.m. during the morning of September 15, 2008, LBHI electronically filed a petition for relief under chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Southern District of New York ("Bankruptcy Court").

The Lehman Bankruptcy Case

The commencement of the chapter 11 bankruptcy case by Lehman was the spark that ignited the simmering economic crisis that began in 2007. The Lehman chapter 11 bankruptcy case represents the largest, most complex, multi-faceted and far-reaching bankruptcy case ever filed in the United States. At the time that the bankruptcy case began, Lehman was the fourth largest investment banking firm in the United States. It had previously reported recorded assets in excess of $600 billion and liabilities of almost that amount. Lehman operated its business pursuant to a classic holding company structure. As the parent corporation, LBHI managed and directed the affairs of the Lehman enterprise. The enterprise maintained a global network of subsidiaries and affiliates with offices in every major financial center in the world that processed many thousands of transactions each business day. At the time of the commencement of the bankruptcy case, LBHI, directly and indirectly, had approximately 8,000 subsidiary entities and affiliates, of which over 100 were actively engaged in the various business activities of Lehman. These activities ranged from derivatives, commercial loans, underwriting, real estate, bank ownership and broker/dealer operations. Through its subsidiaries and affiliates, Lehman employed approximately 26,000 persons immediately preceding the commencement of the chapter 11 bankruptcy case.

LBHI managed the cash generated by the enterprise. Generally, all such cash was swept each night into cash concentration accounts at LBHI and each day LBHI disbursed cash to its various subsidiaries and affiliates, as needed. Lehman's cash needs also were supported by substantial borrowings that created a high debt-to-equity leverage ratio. A large portion of Lehman's borrowings were short term loans which negatively affected Lehman's ability to refinance as the economy slowed and was adversely affected by the 2007 subprime mortgage crisis that continued to expand in 2008

The Lehman bankruptcy was unplanned. As a financial institution, Lehman's viability depended to a large extent on the confidence of the financial markets and the public. Accordingly, the disclosure of bankruptcy consideration and planning would have been disastrous to the continued operations of such a financial institution. Indeed, the public comments by various persons as to Lehman's vulnerability to bankruptcy subsequent to the financial distress of Bear Stearns & Co., in March, 2008, had negatively affected Lehman.

The commencement of the chapter 11 bankruptcy case had immediate and severe consequences. Lehman operated as a global organization with an integrated electronic accounting and reporting system for the many thousands of daily transactions that in the aggregate involved billions of dollars. The bankruptcy filing by LBHI, and the separate, almost contemporaneous initiation of administration proceedings of Lehman Brothers Inc. (Europe) ("LBIE"), the major London based LBHI subsidiary, under the insolvency laws of the United Kingdom, had the immediate effect of a worldwide collapse of the Lehman accounting and reporting system. As a result, the ability to determine the status of transactions and to ascertain assets and liabilities was substantially diminished. Within days of the commencement of the bankruptcy case, approximately 80 insolvency proceedings affecting Lehman subsidiaries and

affiliates were initiated in 18 foreign countries. In those proceedings, receivers or administrators were appointed to oversee and administer the disposition of those entities and their respective assets and liabilities.

As of September 15, 2008, Lehman was a party to over 10,000 derivatives contracts relating to approximately 1.7 million transactions. Lehman was also a major participant in hundreds of substantial real estate and loan transactions. Those investments and transactions in the aggregate involved billions of dollars. The commencement of the Lehman bankruptcy case caused disruptions and systemic consequences in all of those situations. These disruptions abetted the crisis of confidence that occurred after the bankruptcy filing. To a limited degree, however, the ramifications of the Lehman bankruptcy case were alleviated by the ability to use the provisions of the Bankruptcy Code to effectuate the sale of the Lehman North American Capital Markets business to Barclays Capital Inc. ("BarCap").

During the morning of September 15, 2008, negotiations began with BarCap as to a possible sale of Lehman's North American Capital Markets business to BarCap. Those negotiations culminated in the Bankruptcy Court approved sale of that business to BarCap within five days of the commencement of the Lehman bankruptcy case[4].

The sale resulted in the transfer of essentially all of the New York-based Lehman employees to BarCap and enabled the expeditious transfer and satisfaction of customer accounts. It was accomplished because of the ability to effectively use the provisions of the Bankruptcy Code and to obtain the cooperation of SIPC to innovatively coordinate and integrate the

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4 The sale was consummated on September 22, 2008 and involved the transfer of over approximately $47 billion of assets and the assumption of substantial liabilities. Subsequently, LBHI, the SIPA Trustee of LBI and the Lehman Statutory Creditors' Committee joined in proceedings against BarCap challenging the sale or, alternatively, varying aspects of the sale. To date, approximately 17 hearing days have been consumed in those proceedings and it is likely that the hearings will not be completed until October, 2010. Those proceedings are currently pending in the Bankruptcy Court (Case No. 08-13555 and Adversary Proceeding Nos. 09-1731 and 09-1733).

bankruptcy case with the LBI case under the Securities Investor Protection Act ("SIPA") that was commenced on Friday, September 19, 2008 in coordination with the BarCap sale. The sale avoided potentially harsh consequences to Lehman customers and employees. The transfer of the North American Capital Markets business essentially was seamless. The sale enabled the North American Capital Markets business to continue operations on Monday, September 22, 2008. However, it did leave the Lehman chapter 11 bankruptcy administration with few Lehman employees. To overcome this problem and facilitate the administration of the Lehman bankruptcy case, BarCap and LBHI entered into a Transition Support Agreement ("Agreement"). To provide the necessary personnel, for administrative purposes, LBHI engaged Alvarez and Marsal Holdings LLC ("Alvarez & Marsal"). Approximately 180 to 200 employees of A&M became the basic core staff for Lehman. The Agreement, together with the support of A&M and the over $1 billion in cash received as a result of the BarCap sale, enabled the administration of the Lehman chapter 11 bankruptcy case to proceed.

The bankruptcy of Lehman was a catalyst for systemic consequences throughout the world. It fostered a negative reaction that endangered the viability of the financial system. As a result of failed expectations of the financial markets and others, a major loss of confidence in the financial system occurred. The consequences of that crisis of confidence are still a matter of debate and final accounting. Nevertheless, it is abundantly clear that the financial world almost went into a tailspin and is still suffering from the panic that occurred during the fall of 2008.

The actual costs of the Lehman chapter 11 bankruptcy case and other significant facts are:

1. Through July 31, 2010, the cost of administering the Lehman bankruptcy case, based upon the filed operating reports and applications by

professionals for compensation and reimbursement of expenses, but including the costs of the A&M employees necessarily engaged to replace the Lehman employees transferred to BarCap is approaching $1 billion. Those costs include approximately $100 million incurred in connection with the independent examination of Lehman's affairs made by Anton R. Valukas, the Senior Partner of Jenner & Block, a Chicago-based law firm, as the Bankruptcy Court appointed Examiner[5]. There is no current estimate of the future costs of administration. However, it is likely over the next two years the expenses of administration may approximate a like amount.

2. The second anniversary of the bankruptcy filing is approaching and the expected duration of the Lehman bankruptcy case is estimated to be an additional two years or more.

3. Since September 15, 2008, approximately 66,000 claims against Lehman have been filed against Lehman in the bankruptcy case. The gross amount of these claims exceeds $873 billion. Many of the filed claims assert unliquidated damages. Currently, it is estimated that the total allowed amount of claims will be under $300 billion. The process of claims reconciliation is underway, but extremely difficult, as the nature of many of the transactions involved are extremely complex and present numerous difficulties in unwinding.

4. There has been a substantial amount of litigation commenced in the Bankruptcy Court and elsewhere relating to claims and other possible causes of action. Recently, Lehman commenced an adversary proceeding in the Bankruptcy Court against JPMorgan Chase Bank N.A. ("JPMorgan") seeking the recovery of billions of dollars based upon asserted avoidable transfers and other claims. JPMorgan has denied the claims asserted and litigation is contemplated to extend into 2010. As the expiration of applicable statutes of limitations approach, it is anticipated that additional substantial litigation will be initiated[6]. As to derivatives and the complexity associated with such transactions, the Bankruptcy Court has approved the adoption of Alternative Dispute Resolution

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5 In March, 2010, Mr. Valukas filed his Examiner's Report with the Bankruptcy Court. The Examiner's Report, exclusive of exhibits, totals 2209 pages plus approximately 1800 pages of appendices. The Report is a public document. Mr. Valukas was assisted by the accounting firm of Duff & Phelps in discharging his obligations as Examiner. The Examiner's Report includes an extensive section covering Lehman's relationship with government regulators. It is entitled, "The Interaction Between Lehman and the government" and consists of 54 pages. A copy of Mr. Valukas's related written testimony before the Committee on Financial Services of the United States House of Representatives on April 20, 2010 is attached as Exhibit 1.

6 The Complaint and JPMorgan's Motion to Dismiss the complaint filed in the Adversary Proceeding (No. 10-03266 (JMP)) are attached as Exhibits 2.

("ADR") procedures for derivatives transactions. Because of the nature of those transactions, the progress is slow involving extensive discovery. Three independent mediators have been appointed in connection with the ADR process. Thus far, as a result of this process, over $181 million has been recovered for the benefit of the Lehman.

5. There has been no tabulation of the actual and expected costs of administration of foreign insolvency proceedings. However, the costs of the insolvency proceedings of LBIE, as publicly reported, reflect the substantial costs of administration of that case. Those costs are running at a pace that basically parallels the administrative costs of the Lehman chapter 11 bankruptcy case, notwithstanding its smaller size.

6. The extent of the foreign insolvency proceedings directly related to Lehman illustrate the systemic consequences of the Lehman bankruptcy and does not take into account the bankruptcy and insolvency proceedings of other entities that was caused by the Lehman chapter 11 bankruptcy case. In the United States there have been a significant number of bankruptcy cases commenced because of Lehman's financial collapse. Currently there are no statistics as to the number of proceedings commenced by or against non-Lehman entities because of Lehman's failure.

7. The public stockholders of LBHI have lost all of the value of their investments. The general unsecured creditors of Lehman have suffered substantial losses and their recoveries from the administration of the Lehman bankruptcy case will result in very substantial losses of principal. Estimated recoveries will be below 20% of allowed claims.

8. Of particular significance is that the administration of the Lehman bankruptcy case has not directly cost the U.S. taxpayers a single dollar. It is the stockholders of LBHI and the Lehman creditors who are bearing the brunt of the direct costs of the Lehman chapter 11 bankruptcy case.

Was Lehman Too Big To Fail

The phrase "Too Big To Fail" is seductive and somewhat inflammatory. In reality there is no entity that is too big to fail. The real issue is to determine how to deal with potential failure. It is the consequences of failure that must be realistically evaluated. Such evaluation may lead to the loose application of the phrase "Too Big To Fail." Inevitably, there always will be situations in which the consequences of naked failure and collapse of a major entity will so materially affect the economy and the public interests that intervention and

remedial action may be mandatory. That does not mean that the potentially failing entity has to be "bailed out" without loss to its owners and creditors. Rather, the potential systemic risks attendant to failure need to be ascertained and, if appropriate, action taken to ameliorate those risks that endanger the public interests.

In the case of Lehman, it appears that the decision to apply moral hazard was ill-advised. Lehman's bankruptcy precipitated a crisis that almost resulted in the destruction of the financial system. It shocked the financial markets and the investing public. It disrupted thousands of financial transactions on a global basis, with the consequential loss of value.

The Lehman bankruptcy caused a failure of expectations held by the financial markets and investors. Essentially in all prior like situations, the potential affects of contemplated failures were diminished by third party actions such as those taken by the financial community, with the encouragement of the Federal Reserve Bank in connection with the crisis relating to the hedge fund, Long-Term Capital Management, in 1998, or the more recent government action taken in the case of Bear Stearns & Co. The practice of third party intervention to mitigate the potential systemic consequences of failure has a long history. It goes back in recent times to the intervention of the New York Stock Exchange ("NYSE") in the context of the so-called Salad Oil Scandal of 1963 to protect the public customers of NYSE member firms, as well as the creation of the Resolution Trust Corporation to deal with bank failures in the Southwestern United States in the late 1980s. It was reaffirmed with respect to Bear Stearns & Co. and the conservatorships adopted for Fannie Mae and Freddie Mac in September, 2008.

The bankruptcy of Lehman may have directly resulted in the freezing of the financial markets that occurred during the week of September 15, 2008. By Wednesday,

September 17, 2008, the commercial paper market had materially contracted to the point that major U.S. corporations were confronting potential illiquidity. A situation that caused such corporations to be concerned as to their ability to have sufficient cash to meet their obligations. In addition, the viability of firms such as Morgan Stanley & Co., the Wachovia Bank, and even Goldman Sachs & Co. was being questioned during the calamitous days and weeks of September and October, 2008.

It has been estimated by various commentators that during the week of September 15, 2008, over $700 billion of value disappeared. In that perspective, it is reasonable to question the decision of the government to abandon the notion of any conceivable assistance or support for Lehman that would have served to alleviate the potential financial distress and possibly have saved the financial markets from the turmoil that occurred. It did not have to be a "bail out" of Lehman creditors or its stockholders but, rather, a means to mitigate the costs and severe disruptions that resulted from the decision to allow Lehman to fail and commence a bankruptcy case without any government support.

A government sponsored plan to support an orderly wind-down of Lehman's business over a reasonable period of time might have negated or substantially eliminated the risks to the financial system and the public that were actually encountered. It has been estimated by some commentators that a government sponsored wind-down, with limited guaranties, might have cost $40 to $50 billion. That cost would have been far less than the initial $700 billion of value that disappeared during the first week of Lehman's chapter 11 bankruptcy case and the additional costs to the economy that followed in subsequent weeks. In addition, it is conceivable that the costs incurred by the government and others in connection with supporting or saving other entities and the automobile industry might have been substantially less.

Former Secretary of the Treasury, Henry C. Paulson, Jr., and others have made various comments concerning the demise of Lehman. Secretary Paulson has commented that (1) the government did not have the tools to deal with Lehman, and (2) Lehman lacked adequate collateral to secure any government financing. Those comments are not persuasive. On Tuesday, September 16, 2008, the government did find the tools to free up approximately $80 billion as an initial investment in American International Group ("AIG"), and to subsequently increase that amount to over $100 billion. Of course, there may be many facts that are not within my knowledge that may have influenced the government's decision. If so, they have not been substantiated. It is also difficult to evaluate the impact on the Lehman situation on September 14, 2008 of the then developing AIG crisis.

The damages and harm precipitated by the Lehman bankruptcy could have been substantially reduced by innovative actions of the government. Instead, the government miscalculated and the financial system was pushed to the brink of total collapse, as Secretary Paulson subsequently explained to the leaders of Congress in requesting approval of the Toxic Assets Repurchase Program ("TARP"). As a consequence, intervention by the government was once again was recognized as necessary to preserve the national economy and the public interests.

The Government Failure To Provide Assistance To Lehman

The government did not provide any assistance to Lehman. The results are a matter of history. The reasons why the government did not provide assistance to Lehman has been the subject of speculation by many authors and others. The failure of the government to provide assistance to Lehman may have resulted from a serious miscalculation of the potential systemic risks that were presented by the proscribed Lehman's failure and collapse.

Possibly the government believed that in September, 2008, the financial markets already had taken into account and were prepared for the eventuality of Lehman's bankruptcy. The government may have assumed that because of all the notoriety created by certain hedge fund spokesmen as to Lehman's financial condition and media reports, that the financial markets and, perhaps the public, had factored into their operations and activities Lehman's potential failure. It is in that context that the government representatives, during the September 14, 2008 meeting, may have assumed that the referenced press releases would adequately serve to calm the financial markets and the public.

The government failed to take into account the expectations that had been created by prior governmental action and the history of third-party interventions in circumstances of financial crises. The government appears to have concluded that during the day of Lehman's bankruptcy it would be tumultuous, widely publicized and disconcerting, but that by Tuesday, September 16, 2008, the concern would have contracted, and by Wednesday, September 17, 2008, Lehman's bankruptcy mostly would be a historical fact. If that was the government's belief, it was a serious miscalculation. Lehman's bankruptcy, as noted, was the spark that inflamed the existing financial distress and may have caused it to quickly blossom into a major debacle. Appropriate intervention may have prevented, or at least materially lessened, the full impact of the financial panic that did occur.

Thank you for the privilege of being able to testify before this Commission.