

MEMORANDUM FOR THE RECORD

Event: Interview of Andrew Feldstein

Type of Event: Phone Interview

Date of Event: May 4, 2010; 12:45 p.m.

Team Leader: Brad Bondi

Location: FCIC Offices, 1717 Pennsylvania Ave., Wash., DC

Participants - Non-Commission:

- Andrew Feldstein, Co-Founder Blue Mountain Capital

Participants - Commission:

- Vic Cunicelli
- Tom Borgers

MFR Prepared by: Vic Cunicelli

Date of MFR: May 4, 2010

Summary of the Interview or Submission:

On the above date and time, reporting investigator (RI) and Senior Investigator Tom Borgers interviewed Mr. Andrew Feldstein. Mr. Feldstein is CEO/CIO of Blue Mountain Capital, an asset management fund with focus in the credit and derivatives markets. Mr. Feldstein was recommended to FCIC staff by William Ackman as an excellent credit analyst who could lend insight to the Commission's attempt to understand causes of the financial crisis. Mr. Feldstein agreed to pass along any potential market participant contacts he believes could help the Commission. Mr. Feldstein **requested confidentiality** on all statements made to Commission staff. Mr. Feldstein said as follows:

Ratings have "power" as they are used the world over and are the basis for various rules regulators use to regulate the capital markets. Inaccurate ratings had such a devastating effect on the economy as a reflection of the power they carry. Rating agencies (RAs) are "outgunned" by banks which have more money, people, talent and negotiating leverage than RAs. The combination of the power of the ratings which RAs produce and the relative advantage of their client banks causes a situation ripe for

exploitation. Banks use their influence and substantial advantage in resources to game the system and have RAs produce ratings in line with banks' desired outcomes. This situation, coupled with explosive growth in structured finance, created an environment of ratings arbitrage where banks could play RAs against one another.

RA models were not necessarily inaccurate. However, the above situation caused RAs to skew inputs (assumptions) to models in order to produce desired outputs for client banks. If RAs were "slaves" to their models, this created additional opportunities for banks to arbitrage the models creating assumptions or structures to optimize desired outcomes that did not necessarily reflect reality. RAs were not more culpable for the current financial crisis than the bankers, investors or regulators. Bankers gamed the ratings. Investors did not perform due diligence. Regulators turned a blind eye to questionable conduct by market participants.

If an RA refused to rate products, it could have slowed or softened the current financial crisis, but would not likely have precluded it. For instance, Moody's could have refused to rate securities it thought presented risk to the system. However, market rules only require two RAs and Fitch and other RAs would gladly have stepped into the void. Moody's could have publicly expressed their reluctance to rate which could have attracted regulatory attention, but could have been equally likely to decimate the company's market position before it ever slowed the market in structured finance.

Going forward, additional regulation will be necessary to shine light on products currently outside the regulatory regime such as derivatives. Legislation will have to produce additional opportunities for disclosure as, 'Markets work best when there is adequate disclosure and market participants can act on disclosure.' The AIG-Goldman matter provides a case study for the need for additional disclosure. AIG sold substantial protection to Goldman (CDS) without disclosing same. Goldman knew of AIG's exposure, other market participants did not. When the market locked and AIG needed a bailout to repay their exposure to Goldman, regulators later asked Goldman why they needed the money. Goldman informed they were hedged (bought protection on AIG) and did not need AIG to be bailed out.