

**Written Statement Of Richard S. Fuld, Jr.  
Before The Financial Crisis Inquiry Commission**

September 1, 2010

Chairman Angelides, Vice Chairman Thomas and Members of the Commission, I appreciate the invitation to appear before you today. I am proud to have spent my entire business career of over forty years at Lehman Brothers and to have been its Chairman and CEO for its last fourteen years.

Lehman's demise was caused by uncontrollable market forces and the incorrect perception and accompanying rumors that Lehman did not have sufficient capital to support its investments. All of this resulted in a loss of confidence, which then undermined the firm's strength and soundness. Those same forces threatened the stability of other banks -- not just Lehman. Other firms were hurt by their plummeting stock prices and widening CDS spreads. But Lehman was the only firm that was mandated by government regulators to file for bankruptcy. The government then was forced to intervene to protect those other firms and the entire financial system.

Looking back, Lehman Brothers grew its business during a period of huge capital accumulation and easy access to liquidity and asset financing. During that time, Lehman Brothers' profitability and balance sheet grew accordingly.

In 2007, when the U.S. housing market began to show signs of weakening, Lehman Brothers and many of its competitors had already accumulated large positions in what were considered less liquid assets. Many market observers, including government officials charged with oversight of the financial markets, believed that the problems in the subprime residential mortgage market were and would be contained.

In retrospect, one can now see that as 2007 progressed, the weakening in the U.S. housing market was worse than predicted and spread to other sectors of the financial system.

Those adverse market conditions accelerated in March 2008 after Bear Stearns nearly failed. I believed then, and still do now, that had the Fed opened the financing window to investment banks just before the Bear Stearns problem, that decision might have provided the necessary liquidity to keep Bear Stearns operational and, more importantly, might have lessened the need for additional government intervention. Still, having acted, the intervention of the federal government set a precedent in the marketplace that impacted liquidity, capital formation and the expectations of creditors and stockholders for at least the next six months. At the same time, the federal government and the individual regulators involved were criticized for using taxpayers' money to rescue a financial company, which then set another precedent of how "not" to handle the next problem.

With Bear Stearns gone, Lehman, as the next smallest investment bank, became the focus of the marketplace and was subject to increasingly negative and inaccurate market rumors.

Critically, in 2008, Lehman reduced its total exposure to less liquid assets by almost 50%, from approximately \$126 billion to \$69 billion. We further strengthened our capital and liquidity positions by raising \$10 billion of new equity.

During that same period, Lehman fully welcomed and cooperated with SEC and Fed officials, who were physically present in our offices monitoring our liquidity, funding, capital, risk management and mark-to-market process. Lehman also proposed to government regulators certain measures that could have helped Lehman and bolstered confidence in the financial markets. Those measures included (i) permitting Lehman to convert to a bank holding company, (ii) granting Lehman's Utah bank an exemption under Section 23A of the Federal Reserve Act to raise deposits, which would have given the firm additional liquidity and (iii) imposing a ban on naked short selling. Each of those requests was denied at the time. Tellingly, though, each measure was later implemented in some form for other investment banks during the days and weeks following Lehman's bankruptcy filing.

Despite all those efforts, unfounded rumors about Lehman continued to besiege the firm and erode confidence. An investment bank's very existence depends on confidence to consummate transactions, pledge collateral and repay loans. Without that confidence, no bank can function or continue to exist. This loss of confidence, although unjustified and irrational, became a self-fulfilling prophecy and culminated in a classic run on the bank starting on September 10, 2008, that then led Lehman to file for bankruptcy four days later, in the early morning hours of September 15.

In broad summary, on Sunday, September 7, 2008, the federal government placed Freddie Mac and Fannie Mae in conservatorship, destroying the value of their recently issued preferred shares. Two days later, on September 9, there were news reports that Lehman's talks with the Korean Development Bank had faltered. That day Lehman's stock dropped 45%. The next day, September 10, Lehman pre-released its third quarter 2008 results. The firm reported a net \$3.9 billion loss, including \$7.8 billion in gross writedowns on its residential mortgage and commercial real estate holdings. Even with this loss, Lehman still reported an equity capital position of \$28.4 billion (\$2.2 billion higher than the previous quarter). Lehman also announced plans to divest \$25 billion of its commercial real estate assets into a separately capitalized entity. More rumors swirled that led the market to believe that Lehman's assets were not adequately marked to market and

that Lehman did not have enough capital to withstand further writedowns. Those rumors proved to be completely false. Lehman's stock dropped further.

The run on the bank then started. Lehman's principal clearing banks demanded that Lehman post additional collateral. Counterparties to the numerous repurchase transactions that Lehman conducted on a daily basis began to withdraw business and to demand increased collateral to consummate trades. Liquidity was frozen by those clearing banks, and hedge fund customers began migrating to other firms.

On Friday, September 12, and through that Sunday, the Federal Reserve Bank of New York held emergency meetings with the major financial institutions to explore financing facilities and strategic alternatives with both Bank of America and Barclays. By Sunday night, Treasury and Fed officials decided not to provide temporary financing or support to any of those possibilities. Lehman then was mandated by government regulators to file for bankruptcy before the Asian markets opened the next day.

Notably, on that same Sunday, the Fed expanded for investment banks the types of collateral that would qualify for borrowings from its Primary Dealer Credit Facility. Only Lehman was denied that expanded access. I submit, that had Lehman been granted that same access as its competitors, even as late as that

Sunday evening, Lehman would have had time for at least an orderly wind down or for an acquisition which would have alleviated the crisis that ensued.

There are a number of completely incorrect claims which have been held up as explanations for the demise of Lehman Brothers. To this day, those incorrect claims still persist in the public domain. Just because those incorrect assertions are repeatedly made does not make them true. I highlight these claims only because I believe this Committee needs to hear what is true:

First, there was no capital hole at Lehman Brothers. In contrast to the false market rumors about Lehman's mark-to-market determinations, even the Lehman bankruptcy examiner found immaterial differences in the firm's asset valuations, ranging from a low of \$500 million to a high of \$1.7 billion. As of August 31, 2008, two weeks prior to the bankruptcy filing, Lehman had \$28.4 billion in equity capital. Assuming a full \$1.7 billion in additional writedowns, as estimated by the examiner, Lehman still would have had \$26.7 billion in equity capital. Positive equity of \$26.7 billion is very different from the negative \$30 or \$60 billion "holes" claimed by some.

Second, Lehman had adequate financeable collateral. Many people, to this day, do not know that on September 12, the Friday night preceding Lehman's bankruptcy filing, Lehman financed itself and did not need access to the Fed's discount window. In addition, on that Monday, September 15, the day of the

filing, Lehman Brothers Inc., the U.S. broker-dealer subsidiary, borrowed about \$50 billion from the New York Fed by pledging acceptable collateral. The Fed was paid back 100 cents on the dollar. What Lehman needed on that Sunday night was a liquidity bridge. We had the capital. Along with its excess available collateral, Lehman also could have used whole businesses as collateral -- such as its Neuberger Berman subsidiary -- as did AIG some two days later.

Third is the notion that Lehman did not do enough to try to seek solutions to the crisis. As I have stated, Lehman made proposals about changes to its corporate structure to government officials, new ways to create liquidity and changes to regulations to prevent continued manipulation of stocks of financial companies. Lehman strengthened its position in 2008 by decreasing its exposure to less liquid assets by almost 50%, by writing down asset values by almost \$25 billion, by raising \$3.8 billion of equity capital more than its total net losses, by cutting its dividend and by increasing its long-term debt. Lehman pursued new capital opportunities with numerous potential investors, potential strategic partners and potential buyers of the firm. Lehman created an SEC-approved plan to spin off certain illiquid commercial real estate assets. Lehman created alternative capital options, which included changing convertible and preferred securities to common stock, further decreasing its less liquid assets, and selling all or part of its Investment Management Division. Those options, taken together, could have

created \$7 to \$11 billion of additional equity capital. In the end, however, Lehman was forced into bankruptcy not because it neglected to act responsibly or seek solutions to the crisis, but because of a decision, based on flawed information, not to provide Lehman with the support given to each of its competitors and other non-financial firms in the ensuing days.

In retrospect, there is no question we made some poorly timed business decisions and investments, but we addressed those mistakes and got ourselves back to a strong equity position with a Tier I capital ratio of 11%. We also had financeable collateral and solidly performing businesses. There is nothing about this profile that would indicate a bankrupt company.

I thank the Commission for its time and look forward to addressing any questions.