IN THE UNITED STATES COURT OF FEDERAL CLAIMS

STARR INTERNATIONAL COMPANY,)
INC., Individually and on)
Behalf of All Others)
Similarly Situated,)
Plaintiffs,) Case No. 11-779C
vs.)
UNITED STATES OF AMERICA,)
Defendant.)
---------------------------------)

Courtroom 4
Howard T. Markey National Courts Building
717 Madison Place, N.W.
Washington, D.C.
Thursday, November 20, 2014
9:30 a.m.
Trial Volume 35

BEFORE: THE HONORABLE THOMAS C. WHEELER

Susanne Bergling, RMR-CRR-CLR, Reporter

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I N D E X

WITNESS:	DIRECT	CROSS	REDIRECT	RECROSS	VOIR
SAUNDERS	8142	8242			

EXHIBITS	FOR ID	IN EVID
Plaintiff's		
Number1189		8170
Number1502		8168
Number2206		8350
Number3228		8287
Defendant's		
Number176		8189
Number293		8165
Number363		8196
Number375		8197
Number426		8184
Number428		8184
Number550		8215
Number894		8225
Number974		8150
Number976		8196
Number1308		8166

EXHIBITS	FOR ID	IN EVID
Defendant's		
Number1399		8148
Number1431		8170
Number1442		8189
Number1443		8187
Number1615		8156
Number1893		8187
Number1894		8187
Number1896		8189
Number1898		8233
Number1901		8172
Number1924		8180
Number2701-2768		8241
Joint		
None		

*All exhibits premarked for identification prior to trial.

*See full attached list of admitted exhibits following transcript.

P R O C E E D I N G S

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(Proceeding called to order, 9:30 a.m.)

THE COURT: Good morning. Please be seated.

ALL COUNSEL: Good morning, Your Honor.

THE COURT: We are on the record for day 35 of the trial in Starr International Company versus United States.

Before we bring the witness on, I know we have a couple of issues related to Plaintiffs' rebuttal case. With regard to Mr. Millstein, I looked at the cases that Mr. Gardner gave me yesterday, and I received a proffer from the Plaintiff, and I think based upon those authorities and the submissions, the proper thing to do is to admit the excerpts of the deposition under Rule 32 and as an admission by a party-opponent, and there's no reason for Mr. Millstein to come here and testify. We'll just take the excerpts, and you can submit them as an exhibit, just give it a Plaintiffs' trial exhibit number --

MR. BOIES: We will do that, Your Honor.

THE COURT: -- and we will take it.

MR. DINTZER: Can we be heard on --

MR. GARDNER: Yeah, I -- Your Honor, I understand you have made a ruling, but I think for the record I would like to make a few comments, if you would permit.

THE COURT: Sure, go ahead.

MR. GARDNER: Plaintiffs -- I have read what Plaintiffs' have submitted, and the problem the Plaintiffs' submission is it fundamentally misunderstands the Federal Rules of Evidence. Even under Rule 32, there still has to be a basis to admit it consistent with the Federal Rules of Evidence.

They cite to the hearsay exceptions under Chapter 800 of the Federal Rules. We have never disputed whether it is or is not hearsay. The argument, Your Honor -- and this is what the case law supports -- is that the 600 series, personal knowledge and competence, need to also be satisfied, because obviously, in order to testify, it has to be competent personal knowledge and there has to be a hearsay exception. They have only gotten through one of those two hoops.

They then come back and say, well, wait a second, we can use the depositions from other cases. The problem there, though, is if you look back again at Rule 32, it says you can only use depositions from other cases if the same parties were involved. I don't think there's any dispute here that the same parties were not involved in Brookfield and Murray, as in this case. So, that is a separate evidentiary problem the Plaintiffs have to designate that testimony.

Plaintiffs also argue that, well, of course, Mr. Millstein must have personal knowledge, but I understand them to be saying because he was involved in a later period of time, he somehow understands what happened on the 16th. They don't cite to any deposition testimony for that proposition, and it's my understanding he doesn't have personal knowledge; in fact, he started in May 2009.

So, not only do we have the competency evidentiary problems and not the same party problems, so we have Rule 32 issues there, but then we also do have the notion that he truly doesn't have personal knowledge, and to the extent the Court does admit this, it certainly shouldn't admit it as the admission of a party-opponent because of the failure to establish the predicate of personal knowledge.

THE COURT: Well, look, the gentleman is a high-level official in the Treasury Department. He was involved in restructuring. He made statements on the record regarding AIG. And what is the point of a Rule 30(b)(6) deposition of an opponent if you can never really, you know, use the information later?

MR. GARDNER: I'll tell you exactly what the purpose is, Your Honor, and, in fact, this comes back to what we were talking about about AIG and Mr. Reeder --

THE COURT: I don't want to pursue this anymore.

MR. GARDNER: That's fine, Your Honor. Then will we have the opportunity to counter-designate?

THE COURT: No, I don't think so, because this is not a situation where the witness is unavailable. You know, it's not a similar situation. The Plaintiff has identified segments that they believe can be admitted as an admission, and that's how we're going to treat it.

MR. GARDNER: We understand, Your Honor.

THE COURT: So, that's what we're going to do. And plus, there's lots of evidence in the record on these subjects already. This is not the last word.

MR. GARDNER: Well, but that's why it's not rebuttal, Your Honor, I agree with that sentence completely. I understand your position, Your Honor.

THE COURT: All right, thank you.

MR. DINTZER: The next subject is experts and the Plaintiffs' suggestion that they would like to bring either Mr. Cragg or Mr. Zingales or both of them for a rebuttal case. And at the close of testimony yesterday, we asked and the Court agreed that we should get a proffer so that we would know what's on the plate, so we could choose -- to see if we needed to challenge the nature and also so we could start our preparation.

If I could, Your Honor, I'd like to hand out -- and I'm not sure if the Plaintiffs sent this to the Court, but I would like to hand out what they sent to us so we can talk about that.

THE COURT: Sure.

MR. DINTZER: Thank you, Your Honor. May I approach?

THE COURT: Yes.

MR. DINTZER: So, the first thing, Your Honor, is that this is not a proffer. It's an identification of topics that they would like to rebut, but they do not tell us what testimony they plan to proffer. If there was an expert -- let's say, hypothetically, they had an expert report, we would know what evidence one or the other of these gentleman would be providing, and we would have the ability to actually prepare to counter or at least challenge this stuff, whatever we disagreed with.

Instead, all they've done is listed topics which one or the other might testify about. We don't even know which one. So, we can't even prepare for each individual, depending on which one they've identified.

And the fact that the day before, you know, we're supposed to -- we anticipate closing our case, they don't even know which expert -- I mean, if they haven't reached that point, how can we possibly reach the point of preparation for crossing these individuals? So, that's just -- as a starting point, they're not giving us the information to make this fair.

And I'm going to walk through some of the topics on this. Some of them they have been anticipating since the first weeks of trial, since in the middle of their case. So, they can say, well, you know, the expert just popped up and said something, but some of this goes so far back that the fact that they don't know who's going to respond to it and they can't give us a real proffer on that suggests that they haven't put together the information to make this a fair discussion regarding the proffer -- I mean regarding their rebuttal case.

THE COURT: When do you plan to close your case?

MR. DINTZER: It is our anticipation that we plan to close tomorrow. I have got to check my memory to make sure I know which day it is. Is it Wednesday? So, we do plan to close tomorrow if tomorrow is Friday, Your Honor.

And so -- and so with that thought, the possibility -- now, the second thing to note is that these are very broad, and there's 13 of them, and -- now, I don't know how broadly they actually intend to have their experts respond, but I'm sure the Court would anticipate that we would want a full-blooded opportunity to cross examine whatever issues they open, and so even if on these broad subjects they pinpoint the issues they would like, a full-blooded cross exam on these 13 topics would be thorough and time-consuming.

And the third thing that we would draw the Court's attention to -- and I would like to point out on a couple of these specific topics -- is that the Court has heard a lot about these topics already, and dare I say that since the word "PDCF" comes up on at least one of these, the Court may have heard more than the Court wishes to hear about some of these topics.

So, with that, I would at least like to walk through a couple of these --

THE COURT: Can I interrupt you, Mr. Dintzer?

MR. DINTZER: Yes, Your Honor.

THE COURT: Here are my thoughts at this point, and then if you want to say some other things, that's fine.

As you correctly point out, we have heard a lot of testimony from experts and we still have a little bit more to hear, maybe even more than a little bit, but I'm sure that Dr. Saunders will provide thorough testimony for much of today and then we will hear from --

MR. DINTZER: Professor Daines.

THE COURT: -- Professor Daines tomorrow, and it's not especially remarkable to me that Plaintiffs' experts and Defendant's experts disagree with one another. That's the nature of these proceedings. We have had a lot of testimony.

I don't want to have experts take the stand again and tell me things that they have already told me before. There is some satisfaction, I suppose, in getting the last word, like "I finished the trial on a high note because my expert got a chance to say things," but I don't want to hear things that we've already heard before.

So, it should be -- it should be brief, and I perhaps will be more assertive about saying, "Look, that's not rebuttal; let's get to the point here." But I think with your plan to close tomorrow, I think realistically we'll allow for the rebuttal case on Monday, and then that way you will have the weekend to prepare perhaps further, have a better chance than having to do it on the fly.

And I think that Plaintiff, between now and the end of the day tomorrow, will, I'm sure, give you better information, too, than just this outline of topics. So, I think that's the way I'd like to proceed.

MR. DINTZER: And we understand that, Your Honor. Some of these topics that they anticipate calling rebuttal is -- are them rebutting fact witnesses. They're not addressing what experts have said. They -- and if I could just draw the Court's attention to one just as an example. I have only scratched the surface myself, we got this at 10:00 last night, but if I could just draw the Court's attention to one just as an example, Your Honor.

So, item number 4, "The Government's contention (including through Mr. Offit) that there was no material difference between warrants and preferred stock." Now, first of all, Mr. Offit said he didn't believe that there was a difference between warrants and preferred stock. Now, if they're going to call an expert, I believe Mr. Cragg has already said that he is not in the business of saying what somebody else -- in fact, he can't -- what somebody else really believed.

So -- and to the extent that in the Plaintiffs' case in chief, it came out from a number of witnesses that some people just -- it didn't matter to them one way or the other, we can't see that as proper grounds for rebuttal testimony by an expert on what these people did or didn't believe. And so --

THE COURT: I think I can tell both you and the Plaintiff on this subject, I don't really need to hear anything else about the difference between warrants and preferred stock. I have a good handle on that. I understand that there is a difference, and we don't need to hear further about that.

MR. BOIES: Thank you, Your Honor.

THE COURT: We also do not -- I mean, I'm just looking at these subjects. I don't need to hear anything more about Dr. Mordecai's windows study and events study. I think we have had enough on that. I don't really need to go there.

MR. DINTZER: How about the E and F, Your Honor? That was going to be the next place I was going to go. That's number 1. What happened there is Mr. Schreiber, in his deposition, provided that -- more or less the same testimony he provided on the stand, which is that he believed that -- in fact, I can actually show the Court his deposition if the Court's interested, but basically that he believed that -- that there was -- this is what he said in his deposition:

"The Treasury could have just said, well, no, we're going to exchange our -- we'll get 80 percent of the company" -- that's with the Series C -- "and then we are going to exchange the 49 billion, however much TARP was left over, exchange it for whatever the current stock price of AIG's common stock was at the time." So, he's talking about the order, and then he talked about that same thing when he was on the stand.

These were fact witnesses, and they had Mr. Schreiber on their "may call" list, and none of that was a surprise. To have had an expert now come in and offer testimony about the order of conversion -- that's what he's talking about, whether you convert the C before the E and the F or the other way around -- and to have an expert, as Plaintiffs -- they don't tell us what they're going to say or which expert, but they do say that they want to address this factual testimony with an expert.

I mean, that would be an example, Your Honor, of something perhaps the Court has heard a lot about and doesn't need to hear any more.

THE COURT: I would be happy to hear a little bit of information about that, not too much.

MR. DINTZER: Okay.

THE COURT: I think it might -- that might be helpful. Maybe I can just go through the list.

MR. DINTZER: Could we do that, Your Honor?

THE COURT: Sure.

MR. DINTZER: Because each of these topics, quite honestly, is hours of prep for us to prepare for cross, and so if we could eliminate some of the -- for example --

THE COURT: Okay. So, 3 is out and 4 is out.

MR. DINTZER: We've discussed the credit lines, and I believe those were just factual statements by certain witnesses as to the significance -- as to the fact that lines were drawn down on the 16th.

THE COURT: I really think that's a fact issue.

MR. BOIES: It is, Your Honor, essentially a fact issue, but it is an issue that -- in terms of parsing through all of the material, I think expert testimony -- brief expert testimony is helpful on that.

What we have had is an assertion that all of the lines were drawn down, as the Court will recall, and there was testimony that the Government elicited that said Mr. Willumstad said, "I'm going to draw down the lines," and then he was told, "No, don't do that," but he went ahead and did it anyway.

In fact, that's not true. In fact, certain lines were drawn down and certain lines weren't, and I think an expert identification of what those are, although it's brief, would be helpful to the Court.

MR. DINTZER: Could I be heard on that, Your

Honor?

THE COURT: Yeah. I mean, I -- I suppose I'm willing to hear a little bit about that, but I -- I think I have the impression that some of them were used and some of them weren't.

MR. BOIES: And, Your Honor, this testimony -- I mean, as I've said from the beginning, it's going to be, like, three hours of testimony. This is going to be very targeted testimony, but with respect to something like that where I think the qualitative judgment is probably there, some quantification of that would be helpful to the Court. If not, we won't do it, but I think that --

THE COURT: I'll take a little bit of evidence on that. That's fine. So, that's okay.

MR. DINTZER: Number 6, Your Honor, I can show the Court where the Court has heard about -- I mean, it's even in Mr. Cragg's report, about the benefits of the PDCF and the holding companies. And so I would suggest, Your Honor, that that's something that we've heard hundreds of pages of testimony about.

MR. BOIES: Your Honor, we don't need to talk about the PDCF. However, what the Government elicited was the assertion that membership in the Federal Home Loan Bank system would not have been of material help to

AIG because the savings and loan that AIG had was a small savings and loan.

Now, in fact, what it's possible to do is to -- once you have membership, either as a bank holding company or a commercial bank or as a savings and loan in the FHLB system, you can transfer a lot of assets into that entity and then use those assets to borrow money. So, the actual size of the entity is not decisive.

And one of the pieces of expert analysis on that is that what Goldman Sachs did was they became a bank holding company overnight. They didn't even have a bank holding company before that, and what they did in days -- maybe in a single day but certainly in a very few days -- is they dumped enough assets in there, transferred enough assets from those subsidiaries, to make that a $150 billion entity that they could then draw all that money from the discount window.

So --

THE COURT: But AIG didn't do that.

MR. BOIES: No.

THE COURT: I mean, they didn't even apply or pursue these avenues.

MR. BOIES: Well, but one of the things that they did do, as I think the Court knows, is they did ask whether they could become a bank holding company, and they were told no, and the question is, would that make any difference? And, again, this is -- this is something that takes probably less time to elicit on the stand than --

THE COURT: Than we're talking about it now?

MR. BOIES: -- than talking about it.

MR. DINTZER: Of course, Your Honor, counsel is not including the time for cross examination to clarify what may be elicited on -- if I could direct the Court to Dr. Cragg's original report about AIG not being provided -- and it's on the screen -- not being provided bank holding company status, as Goldman Sachs and Morgan Stanley -- it's almost exactly what counsel was just referring to -- that is in evidence, because the report is in evidence.

Obviously this was a contested fact, this was something that he has already testified about, and what counsel's describing is either repetitive or it's a new opinion. It's one of those two things. And if it's repetitive, of course, the Court doesn't need to hear it, and if it's a new opinion, then that's really unfair for him to be springing a new opinion on effectively the same ideas that he had already been deposed on and addressed in two reports, his initial and rebuttal report.

So, Your Honor, Plaintiffs can say things very quickly, I don't deny that, but for us to then challenge them and give them a full hearing is more complicated, and sometimes the shorter amount of time that they spend asking the questions, the more time I have to spend thorough -- with a thorough examination.

So, we would ask the Court to conclude, at least on number 6, that we have fully vetted the possible avenues that AIG didn't pursue or for whatever reason didn't apply for -- they didn't actually put in a bank holding company application, as the Court knows -- and not entertain any further testimony.

MR. BOIES: Your Honor, this is very narrow testimony. This doesn't have to do with whether a bank holding company is a good idea, whether they would have been accepted, whether they were told not to apply. All that's been vetted. This just goes to the question that if they had been permitted to do that, would it have made a difference? And that is what they elicited, and that's all we're rebutting.

THE COURT: Well, let me do this. I really want to get back to the expert this morning. I would just encourage you to tailor your rebuttal case very finely. You have heard a few of my reactions. I believe I will take this up to chambers, take this list to chambers during the break, and I may have some further observations about it.

MR. BOIES: And, Your Honor, what we could do -- we did this last night, trying to sort through, you know, what we heard this week. What we can do is we can, I think, go and proffer what we would say on these topics; that is, we can tell the Court and counsel for the Defendant sort of what we would anticipate our people saying. That may allow both the Court to understand the narrow subjects that we will actually address and allow them to do whatever preparation they need.

THE COURT: All right. I think that would be helpful, probably.

MR. BOIES: We will try to do that even overnight tonight so they can have it first thing tomorrow morning.

THE COURT: Okay.

MR. DINTZER: One last thing, since the Court is considering this, Your Honor, to the extent that we do finish -- that we do close our case tomorrow, which we anticipate, but perhaps not at the end of the day, but with the possibility at some point earlier than that, that whatever rebuttal case that they are going to provide, if it takes place -- if they elicit the testimony on Friday, that would provide us an even better chance of knowing what we're addressing and basically working over the weekend so that we have an opportunity to do our job on Monday and finish up as early as possible.

THE COURT: All the more reason to get right to these experts.

MR. DINTZER: I know. Thank you very much for hearing us out, Your Honor.

THE COURT: Sure, my pleasure.

Good morning, Mr. Roberson.

MR. ROBERSON: Good morning, Your Honor.

THE COURT: Good morning. Welcome back to our case, Dr. Saunders.

THE WITNESS: Thank you.

THE COURT: Do you understand that you are still under oath in these proceedings?

THE WITNESS: Yes, I do. Thank you.

THE COURT: All right. Let's go ahead.

Whereupon --

ANTHONY SAUNDERS

a witness, called for examination, having previously been duly sworn, was examined and testified further as follows:

DIRECT EXAMINATION (cont.)

BY MR. ROBERSON:

Q. Would you turn the microphone -- point it more toward your mouth? No, toward your mouth, up a little bit.

A. This is okay.

THE COURT: I think the problems, to the extent there were any yesterday, had to do more with the witness' diction than the volume. I think the volume is fine.

MR. ROBERSON: Okay.

BY MR. ROBERSON:

Q. Professor Saunders, do you remember yesterday we were talking about the sec lending portfolio of AIG relative to other comparable insurance companies?

A. Yes, I do. Yes.

Q. If you look back at DX 2712, just to get to the scope again, do you recall we discussed this slide?

A. Yes, I do.

Q. And it shows the comparison as a percentage of total assets between AIG and MetLife?

A. That's correct.

Q. And so we want to do a little bit -- discuss a little bit more the comparison between AIG and MetLife. So, now, if you would turn to slide DX 2715, and can you tell us what's reflected in this demonstrative?

A. This is the -- it shows in the second quarter of 2008 the valuation losses of AIG versus valuation losses or gains of MetLife, and it's the difference between the price that the securities lending portfolio bought the securities versus the fair value. And as you can see, the -- there's a loss of 8 billion in terms of market value of the underlying -- the underlying securities in that second quarter compared to, say, MetLife, which is the blue bar, which has more value, again, between their value and the purchase price. So, basically, MetLife made a large loss and a small gain was made by MetLife.

Q. You said MetLife twice there, so -- in your last response.

A. AIG, sorry.

Q. AIG had a what?

A. Yes, so if I can just repeat, AIG had a large loss in the second quarter in its securities lending portfolio, over 8 billion, and there was a small gain for MetLife.

Q. Okay. What is the significance of the fact that MetLife reported a valuation gain while AIG reported billions in losses?

A. Well, I think MetLife -- it implies MetLife's portfolio is much less aggressive, because both were subject to the same market forces as of this time, and

MetLife was making a small gain, and AIG was making a large loss.

Q. If Dr. Cragg is correct that marketwide forces were the cause of the liquidity problems in AIG's securities lending program, how should the securities lending programs of other insurance companies have been affected?

A. Well, they should be similarly affected.

Q. And why is that?

A. Because they would both be subject to the same market forces at the same time, and as we see here, comparing MetLife with AIG, we see they weren't.

Q. Now, are you familiar with the term "maturity mismatch"?

A. Yes.

Q. Can you tell us what that is?

A. That's when the assets and liabilities are not of the same maturity for a particular institution. In the case at hand here, the securities lending portfolio of AIG had very short-term liabilities, whereas the asset portfolio was relatively long term.

Q. And how, if at all, does a maturity mismatch affect liquidity risk?

A. If the providers of the funds, i.e., the suppliers of the funds, i.e., the liability side of the portfolio decides to withdraw their funds, then the holder of the assets in which those funds were invested either has to provide cash, either out of its reserves, or sell those assets to meet that withdrawal requirement.

Q. And with respect to the sec lending program, the borrowers of the securities had the capacity to return the securities, right?

A. Yes, and demand cash immediately in return.

Q. It was immediately in return?

A. Yes, because they -- they had very short-term contracts. They could withdraw their funds over very short periods of time. I think the average maturity of the liabilities was in days, whereas the average maturity of the assets was well over five years, I believe.

Q. Okay. And was there evidence of a maturity mismatch in AIG's securities lending portfolio?

A. Yes. As I mentioned, I believe the maturity of the liabilities was a matter of days, might have been -- I can't remember, I think it was a sort of figure of 13 days, whereas the average maturity was around five years on the asset side of the portfolio. So, there was a mismatch. The assets had a longer maturity than the liabilities.

So, if the liability side that provided the funds decided not to renew those security loans to the lending portfolio, lending characteristics, there would be a rollover risk in the sense that the -- AIG would have to respond by selling either assets from its securities lending portfolio or providing cash.

Q. Okay. Now, was AIG downgraded on September 15th, 2008?

A. Yes, it was.

Q. And how, if at all, did the maturity mismatch in AIG's securities lending program impact AIG after it was downgraded on September 15th, 2008?

A. The downgrade affected its liquidity risk because, again, securities lending, the liabilities side, the people providing the funds in return for short-term borrowing of securities, were less willing to roll over their supply of funds to AIG through the securities lending portfolio.

Q. And did the borrowers, in fact, on September 15th and continuing, return securities that had been bought?

A. I believe so, yes.

Q. Significantly?

A. I believe there was a significant decline in the securities lending cash flows from the securities

borrowers to AIG's securities lending portfolio.
Q. Did AIG need funding from external sources to meet demands by counterparties to return their cash collateral during the last half of September of 2008?
A. Yes.
Q. Do you know whether or not MetLife requested a Section 13(3) loan in September of 2008?
A. I believe it didn't.
Q. And what, if anything, does that indicate about MetLife's ability to fund demands by counterparties to return their cash collateral in its securities lending program?
A. Well, they either had some internal cash or access to private sector sources of financing.
Q. Now, please turn to slide 27 --
Well, before we do, Your Honor, we move to admit, under Rule 703, DX 1399.
MR. BOIES: No objection, Your Honor.
THE COURT: Defendant's Exhibit 1339 is admitted with a Rule 703 restriction.
MR. ROBERSON: Your Honor, it's 1399.
THE COURT: I'm sorry, 1399 is admitted with a Rule 703 restriction.
MR. ROBERSON: Thank you.
(Defendant's Exhibit Number 1399 was admitted

into evidence.)

BY MR. ROBERSON:

Q. And what's reflected on slide 2716?

A. This is just a reaffirmation of what I just said about maturity mismatch from S&P, from a rating book that they published on August the 7th, 2008, and there's an insert shown with the yellow coloring, and I'll just comment on what it says.

"AIG invested the proceeds of this program in largely subprime and Alt-A mortgage-backed securities with a duration far longer than the liabilities that they support, which we consider higher risk than most other insurance company programs."

Q. And what is your reaction to S&P's comment?

A. Well, that was consistent with the fact that AIG's securities lending portfolio provided mostly very short-term cash collateral and invested in long-term assets, such as residential mortgage-backed securities.

Q. Now, what else, if anything, did you do to evaluate whether AIG's liquidity problems resulted from marketwide factors or AIG-specific factors?

A. I looked at various metrics from Dr. Cragg that he identified, peer groups of other financial institutions, to see whether they were similarly affected by marketwide forces as AIG was over this

relevant period.
Q. How many of AIG's insurance company peers requested an individual Section 13(3) loan from the Federal Reserve in September of 2008?
A. I'm unaware of any.
Q. What, if anything, is the significance of the fact that other insurance companies did not need a Section 13(3) loan from the Federal Reserve in September of 2008?
A. They either had internal sources of funds or they had access to private sector financing.
Q. Now, can you turn to slide -- excuse me.
I move to admit, under 703, DX 974.
MR. BOIES: No objection, Your Honor.
THE COURT: Defendant's Exhibit 974 is admitted with a Rule 703 restriction.
(Defendant's Exhibit Number 974 was admitted into evidence.)
BY MR. ROBERSON:
Q. Sir, if you could turn to DX 2717, what point are you making here?
A. The point I'm making here is the peer groups identified by Dr. Cragg outperformed AIG based on multiple financial metrics, despite being exposed to the same market forces as AIG.

Q. And what is the implication, if anything, of your assessment that Dr. Cragg's peer groups outperformed AIG?

A. Simply because they were all subject to the same market forces in market -- financial markets, that AIG suffered much more, suggesting that its problems were specific to the firm rather than to the market in general.

Q. And what did you do to compare the performance of Dr. Cragg's peer groups to AIG's performance?

A. I looked at a number of metrics, stock prices, CDS spreads, and rating changes of the peer groups vis-à-vis AIG.

Q. And if you would turn to the next slide, 2718, what financial metric are you addressing in this demonstrative?

A. Here I'm focusing on the stock price of AIG vis-à-vis life insurance peers identified by Dr. Cragg, property and casualty peers identified by Dr. Cragg, and financial institution peers identified by Dr. Cragg, as well as the S&P 500 Index, which is to my mind a key indicator of market factors, that generally market factors would be reflected directly in the performance of the S&P 500 Index.

Q. And overall, how would you describe AIG's stock performance during these time periods to the stock price performance of Dr. Cragg's peer groups?

A. Well, this is showing from the 9th of September through the 16th of September, and as you can see, on each day, there's -- for one, there's a very large negative return on AIG's stock return. If you look at the median for life insurance companies, property and casualty insurance companies, and financial institution peers from Dr. Cragg's group, there was some falls, but nothing of the order that AIG suffered.

And I think the most important thing is if you look at the S&P Index, it only fell on two days, one by 3 percent and one by 5 percent. And overall, over that whole period, AIG's stock price declined 84 percent between September -- September 9th and September 16th, and the S&P's declined by 4 percent.

So, one would say in finance that the negative excess return of AIG relative to the market was 84 percent minus 4 percent, which is 80 percent. In other words, it declined 80 percent more than the market in general, which tends to suggest this was not market forces driving the negative movement of the stock return of AIG.

Q. Okay. Let's move to your second metric. If you would turn to DX 2719, what metric are you evaluating in this demonstrative?

A. Here's the credit default spreads of various financial sector firms that were viewed as being peers to AIG, as well as AIG itself.

Q. What are credit default swap spreads, CDS spreads?

A. I think I explained them earlier, in an earlier demonstrative. These are the spreads that are required to provide insurance against the default risk of a particular corporation.

Q. And what's the difference between the CDS spreads in this demonstrative and the multisector CDSs that we discussed earlier?

A. This is the cost of providing insurance by a seller of insurance against the risk that AIG may default.

Q. And the earlier discussion was?

A. Where AIG was a writer of insurance against other companies defaulting or, in particular, CDOs defaulting.

Q. And what does the size of the spread reveal about the market's belief about a company's risk profile?

A. The higher the spread, the more costly the insurance against default risk, so it suggests that either the severity of loss or the probability of default are high.

Q. And what is illustrated on the chart on this slide, if you could just walk us through this?

A. This is showing between the 1st of September through the 19th of September the credit default swap spreads of AIG versus six peers that Dr. Cragg identified: Bank of America, Citigroup, Goldman Sachs, JPMorgan, Merrill Lynch, and Morgan Stanley.

Q. And why did you use the five-year CDS spread?

A. This is generally thought to be the most liquid of all CDS spreads.

Q. And how does AIG's five-year spread compare to the other six companies identified in the chart?

A. As you can see on the 16th -- over the whole period, in fact, it was above the peer group spreads -- CDS spreads, suggesting a high default risk over the whole period from the 1st of September, 2008, to the 19th.

Q. And when did AIG's five-year CDS spread peak?

A. As you can see on the 16th, it's peaked at 3500 basis points or 35 percent.

Q. And how would you characterize a CDS spread of 3500 basis points?

A. It would suggest there was a higher risk of

default on AIG's unsecured debt.
Q. And what about the severity of the potential loss?
A. Well, that would be reflected in the 3500 basis points.
Q. How did AIG's five-year CDS spread on September 16th, 2008, compare to the CDS spread of the other six companies on that same day?
A. Well, as you can see by the circle, the other companies, the other six peer group comparators, their maximum CDS spread was around 750 basis points or 7.5 percent.
Q. And what's the significance of that difference?
A. Well, it's indicating that AIG's risk was much higher than these peer group companies as perceived by the sellers of credit default swap insurance.
Q. Now, what was AIG's five-year CDS spread on September 17th, 2008?
A. Well, after the liquidity provision on the 16th in the evening, you can see that it fell to 1821 basis points or 18.21 percent.
Q. And the reason for that fall?
A. Well, again, because of the rescue through the liquidity provision by the Federal Reserve Bank of New York.

MR. ROBERSON: Your Honor, we move to admit DX 1615 under Rule 703.

MR. BOIES: No objection, Your Honor.

THE COURT: Defendant's Exhibit 1615 is admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 1615 was admitted into evidence.)

BY MR. ROBERSON:

Q. So, Professor Saunders, let's move to your next metric, which is at DX 2720, and can you tell us what metric you're analyzing in this demonstrative?

A. In this demonstrative I'm looking at a third metric to see whether market forces were explaining AIG's problems vis-à-vis the peers, and I'm focusing on rating agencies' ratings, S&P and Moody's, which are the two major rating agencies.

Q. What are credit ratings?

A. They're opinions of the rating agencies about the credit quality of a particular borrower, reflecting its ability or willingness to pay its debts as they come due, and obviously the lower the rating, the lower the opinion regarding the credit quality of the particular firm.

Q. And how did you analyze this financial metric?

A. Well, I noted that between December 2007 and

September 16th, 2008, AIG was downgraded four notches by S&P and three notches by Moody's. Then I went on to look at insurance companies and financial institution peers in the green box to see how many of those were downgraded either three notches by Moody's or four notches by S&P over the same interval of time.

Q. And before we discuss the differences in those, how did you determine which of these companies were AIG's peers?

A. I took, again, Dr. Cragg's peer groups.

Q. Okay. Now, what -- what financial institutions were downgraded by S&P and Moody's?

A. First are the insurance peers.

Q. Okay. Do you want to discuss those?

A. Yes. And the insurance peers, there were 12 of them, and none of them were downgraded three or more notches by S&P or Moody's.

Q. And now with respect to the financial institution peers?

A. With respect to the financial institution peers, as you see, S&P downgraded two of the 21 by three or more notches and Moody's one of the 21 peers -- financial institution peers.

Q. And what financial institutions were downgraded by S&P and Moody's?

A. Lehman and Wachovia.
Q. And what happened to Lehman and Wachovia during the last half of September 2008?
A. Well, I think Lehman we know filed on the 15th, and Wachovia was taken over -- had serious distress problems and was taken over by Wells Fargo towards the end of September.
Q. How many -- you know, we have already discussed the insurance peers, and just to reiterate, how many of those were downgraded during this period between December 2007 and September 2008 as much as three notches or more?
A. If I add the two up, we see that only two of the 31 insurance companies plus financial institution peers, were downgraded by S&P by --
THE COURT: It's thirty-three, though, right?
THE WITNESS: Thirty-three, Your Honor, right, 33. Only two of the 33 were downgraded by S&P, and one of the 33 by Moody's, by three -- more than three notches.
BY MR. ROBERSON:
Q. Including both the insurance and financial institution peers?
A. Yes. I just summed the two together.
Q. Right.

Now, how much, if at all, would deteriorating market conditions account for differences between AIG's credit rating performance and the performance of Dr. Cragg's peer groups?

A. Well, as you see, AIG was downgraded far more than any other financial institution or insurance company, other than Lehman and Wachovia.

Q. And what would that indicate to you?

A. Well, that market forces alone could not explain the poor performance of AIG.

Q. Let's turn to your next slide, which sets forth your primary opinion three, and can you remind us what your third primary opinion is, Professor Saunders?

A. AIG could not meet the requirements to become a primary dealer, and in any event, access to the PDCF would not have solved AIG's liquidity crisis.

Q. What is the basis for your opinion that AIG could not meet the requirements to become a primary dealer?

A. Well, the Federal Reserve Bank of New York set forth various criteria to become a primary dealer, and I looked at that criteria. I -- my opinion is it wasn't satisfied by AIG. In other words, they were not able to satisfy the basic criteria to become a private -- a primary dealer.

Q. And if you could turn to slide 2722, can you explain to us what you're setting forth in this slide?
A. Well, the -- the first condition I'm looking at was the number of qualifications about whether you can become a primary dealer or not is the capital that's needed to become a primary dealer, because this capital is there to protect the financial institution against losses. And as you see in the top box, the minimum absolute level of capital for a commercial bank to set up as a primary dealer would be $100 million, and for broker-dealers, $50 million in capital.
Q. And where did you find or what's the source of information you relied upon regarding the capital requirements for primary dealers?
A. Again, this is on the New York Fed Web site on requirements for primary dealership.
Q. Now, do you recall which AIG subsidiary was considering becoming a primary dealer?
A. I believe it was AIGFP.
Q. Now, did FP meet the minimum capital requirements to become a primary dealer?
A. What you see in the white box is GAAP capital as of June 30, 2008, negative 18.9 billion.
Q. What about AIG, the parent company?
A. Its capital was negative 13.5 billion.

Q. And, therefore, did it meet the requirements -- the minimum capital requirements to --

A. Well, neither clearly met the capital requirements.

Q. Now, did AIG outline any plans to become a primary dealer?

A. Yes. I think beginning in September, it did start to outline plans to become a primary dealer.

Q. And did any of AIG's plans address how AIG or AIGFP would meet the minimum capital requirements?

A. Not that I'm aware of.

Q. Now, are there other -- any other requirements that potential candidates had to satisfy in order to become a primary dealer?

A. Yes. Generally, there's three other criteria. One is on the volume of trading, you have to be active in a volume of trading, especially in your interactions with the Federal Reserve Bank of New York's trading desk, largely because primary dealers transmit monetary policy through change in the money supply through primary dealers to the rest of the financial markets by their transactions with primary dealers.

Second, you have to partake in a regular fashion in auctions of treasury bills and treasury bonds. AIG had no issues of treasury bills or treasury bonds.

Third, you had to have relationships with other market participants and feed that information about market appetite for treasuries back to the Federal Reserve trading desk to, again, allow them to consider the market's appetite in making their monetary policy decisions.

So, in other words, primary dealers play a key role in the transmission of monetary policy from the Fed through its trading desk to the rest of the financial system and then ultimately to the economy.

Q. And what sources are you relying upon for the information about the three requirements that you've just described?

A. Again, the Federal Reserve Bank of New York's Web site, which has a description of these qualifications to become a primary dealer.

Q. Did AIG or AIGFP satisfy any of these requirements in September of 2008?

A. No, they did not.

Q. How long did AIG expect it would take before FP could meet the trading requirements to become a primary dealer?

A. I think maybe the minimum that was discussed in one board meeting by Mr. Willumstad was two months, but I think there were other conversations that the Fed had

with AIG suggesting between six and twelve months.
Q. And what is your understanding as to why AIG expected it would take months before it can meet the requirements to become a primary dealer?
A. Well, it's a nontrivial thing to set up a real trading program in treasuries. You have to establish a trading platform, which is the software and the hardware to do the trading. You have to hire a number of traders to -- who are experienced in trading. You need a back office for clearance and settlements. Of course, then you need to have relationships with other financial institutions that want to feed their trades through you.
If you're a primary dealer, you're acting as an intermediary between the market and the Fed. So, you need really to have some relationships with outside parties as well. So, it's not a simple thing just to open a primary dealer.
Q. Okay. And when you began your description, did you say it's a nontrivial thing?
A. I said it's nontrivial. I didn't say it's trivial.
Q. Yeah, I know. I just --
A. It's nontrivial.
Q. Okay. Are you familiar with Dr. Cragg's analysis of the amount of excess liquidity AIG's

insurance subsidiaries could have generated if they had been provided access to the PDCF?
A. Yes, I am.
Q. Have you seen any evidence indicating that AIG requested that its insurance subsidiaries be given access to the PDCF?
A. No.
Q. Were any insurance companies given access to the PDCF?
A. No.
Q. And what is your understanding of the purpose of Dr. Cragg's analysis of providing AIG's insurance subsidiaries access to the PDCF?
A. I think his view is that if you could borrow -- use the assets that are available to go to the PDCF, they would be able to meet the run on the securities lending collateral by the providers of that collateral.
Q. You said they would be able to make a run?
A. No, meet the run.
Q. And what did you mean by that?
A. Cover the run. In other words, more than -- borrow enough to meet the run means basically they would have an excess liquidity even after the run had occurred.
Q. And when you're talking about the run, are you

talking about the return of the --

A. The return of the collateral borrowing to the securities lending borrowers.

Q. Okay.

We'll move to the next slide, but before we do, I would like to move in, under 703, DX 293.

MR. BOIES: No objection, Your Honor.

THE COURT: Defendant's Exhibit 293 is admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 293 was admitted into evidence.)

BY MR. ROBERSON:

Q. Now, if you would move to DX 2723, what conclusions did you reach with respect to Dr. Cragg's claim?

A. Dr. Cragg's analysis of the ability of AIG's insurance subsidiaries to borrow from the PDCF to meet the liquidity demands of AIG's securities lending portfolio is counterfactual.

MR. ROBERSON: One moment, please.

(Counsel conferring.)

MR. ROBERSON: For bookkeeping, I need to get another document moved in. Under Rule 703, back on 2722, I would like to move in DX 1308.

MR. BOIES: No objection, Your Honor.

THE COURT: All right. Defendant's Exhibit 1308 is admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 1308 was admitted into evidence.)

BY MR. ROBERSON:

Q. I apologize, Professor Saunders, for the interruption.

So, we were just discussing slide 2723. If you would go to slide 24, can you describe what you're illustrating with this demonstrative?

A. 2724 is the -- it's reflecting the counterfactual about Dr. Cragg's claims, because AIG developed a securities lending contingency plan. The one -- the latest one prior to the rescue was the one on September 5th, 2008, and in the plan, basically a contemplation for funding to meet a run on their securities lending collateral was the Federal Home Loan Bank borrowings, establish a line from the Federal Home Loan Bank, and/or private sector repo lines.

Q. Now, were the insurance subsidiary assets that Dr. Cragg claims could have been pledged to the PDCF eligible collateral for the repo markets?

A. Yes.

Q. What was the borrowing activity on the PDCF by all primary dealers in the months leading up to the

Lehman Brothers bankruptcy?

A. It was virtually zero. It was a minimal bump. It was virtually zero over that period of three or four months prior to the -- to the Lehman Brothers failure.

Q. And what does that suggest, if anything, about the ability of primary dealers to engage in repo transactions in the private sector market?

A. That primary dealers were okay in borrowing from the private sector market. They had access to the private sector market.

Q. And what does that suggest, if anything, about the ability of AIG's insurance subsidiaries to engage in repo transactions in the private sector markets?

A. Well, if they had repo-type collateral, then they could have engaged in private sector repo transactions. They did not need to rely on PDCF borrowing.

Q. And what does that indicate with respect to Dr. Cragg's theory?

A. Basically, they could have -- if they had enough collateral, they could have gone to the private sector market and engaged in collateral -- in repo transactions, and they did not need to have access to the PDCF to do that.

MR. ROBERSON: Your Honor, before we move on, I would like to move into evidence PTX 1502 under Rule 703.

MR. BOIES: No objection, Your Honor.

THE COURT: Plaintiffs' Trial Exhibit 1502 is admitted with a Rule 703 restriction.

(Plaintiffs' Exhibit Number 1502 was admitted into evidence.)

BY MR. ROBERSON:

Q. And I think we've sort of skipped over -- we have already discussed 2725.

A. Yes. This is -- basically I'm just saying here that prior to Lehman, they did have access to the private repo market if they had any excess collateral, and they could have used that. So, they did not need to use the PDCF prior to Lehman.

Q. Okay. Now, if you move to DX 2726, what is illustrated on this slide?

A. Dr. Cragg makes a claim about the access to the PDCF would have solved their problems should there be a run on the collateral provisions by the securities borrowers if they wanted their cash back, and there is two issues identified that in my mind are important.

First, he doesn't really identify who would be the primary dealer. There's a variety of possibilities. In theory, at least, one he might be thinking about, each of the insurance subsidiaries who are members of the securities lending program, AIGSL, which was the central body to which the securities lending portfolio went through, AIG itself, and or AIGFP. So, it's not well defined or defined at all in his hypothetical about PDCF borrowing.

And the second, I think very important, is that there are regulatory restrictions, very stringent regulatory restrictions restricting the ability of the -- of insurance companies to make loans to affiliates; in other words, to upstream funds to AIG or AIGFP or AIGSL to meet runs on a securities lending portfolio or even to transfer funds between each other, between the insurance subsidiaries themselves.

So, these restrictions are very -- and they make sense, because insurance regulators want to prevent cash deficiencies within a particular insurance company so they can always meet the policyholders' claims, and if they don't have enough cash on hand because they have lent it to somebody else, then that creates a problem. So, there are very strict restrictions on interaffiliate lending from insurance subsidiaries that are in place currently and at the time, of course.

Q. And why is the ability to transfer cash out of the insurance subsidiaries relevant to Dr. Cragg's analysis?

A. Well, he believes that they can, and he just aggregates across the different affiliates in the securities lending portfolio and doesn't take into account these interaffiliate restrictions that are quite binding.

Q. Okay.

And before we move on, I'd like to move into evidence from DX 2726 PTX 1189 and DX 1431.

MR. BOIES: These are subject to 703?

MR. ROBERSON: Of course.

MR. BOIES: No objection.

THE COURT: Okay. Plaintiffs' Trial Exhibit 1189 and Defendant's Exhibit 1431 are admitted under a Rule 703 restriction.

(Plaintiffs' Exhibit Number 1189 was admitted into evidence.)

(Defendant's Exhibit Number 1431 was admitted into evidence.)

BY MR. ROBERSON:

Q. If you could move to the next slide, 2727, can you describe what you're illustrating in this demonstrative?

A. This is an email from Patricia Mosser to other people in the Federal Reserve Bank of New York, and it follows a meeting they had with AIG, senior executives of AIG, as you see below, including Jacob Frankel, the vice chair, and Steven Bensinger, and this confirms the fact that liquidity was really trapped because of these restrictions on interaffiliate transactions within the insurance subsidiaries themselves.

In other words, they couldn't use this to upstream funds or use -- or make loans within -- within the insurance industry subsidiaries. And if I read the quote from the email, it says, "Mobility of liquidity, most cash within the organization is 'trapped' in regulated entities and is not freely transferable to AIG holding company or AIG Financial Products." Then it goes on to say, just below, "but little ability, in general, to use subs to upstream liquidity to holding company or its non-related subsidiaries."

Q. Now, what is your understanding of who provided Ms. Mosser with the information about AIG's trapped liquidity problem?

A. It is coming from the meeting they had with AIG on September the 12th, 2008.

Q. Now, did you analyze how much liquidity AIG's insurance subsidiaries had that was not trapped at the insurance subsidiary level?

A. Yes. I looked at the securities lending contingency plan of September the 5th, 2008. There it sets out the free collateral that's not trapped.

MR. ROBERSON: Before we move on, I want to move into evidence DX 1901 under 703.

MR. BOIES: No objection, Your Honor.

THE COURT: Defendant's Exhibit 1901 is admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 1901 was admitted into evidence.)

MR. ROBERSON: And if I could have PTX 5354 to hand up, please.

May I approach?

THE COURT: Yes.

BY MR. ROBERSON:

Q. Professor Saunders, what is your understanding of what this demonstrative is?

A. This is from Dr. Cragg, and it's his view about the collateral that could have been obtained from the PDCF to meet potential security lending runs by the collateral providers.

Q. How many insurance subsidiaries does Dr. Cragg include in his analysis?

A. He includes 13, these ones along the bottom.

Q. Now, can you describe what the blue and orange bars represent?

A. The blue bar is the amount of collateral it could have used to borrow funds or get loans from the PDCF.

Q. According to Dr. Cragg?

A. According to Dr. Cragg.

Q. And the orange bar?

A. Is the securities lending collateral that was lent to them. So, the red bars is the securities lending collateral, the balances owed to the counterparties, and the blue line is how much they could have borrowed from the PDCF in his opinion.

Q. And how does Dr. Cragg calculate the amount of excess liquidity that would have been available if these 13 insurance subsidiaries were provided to the PDCF?

A. Well, he takes the difference between the blue bar and the red bar and uses that as excess collateral.

Q. Now, did AIG conduct its own analysis of how much liquidity could be transferred out of the insurance subsidiaries?

A. Yes, it did.

Q. And do you know when they performed that analysis?

A. As I mentioned, the most -- the one closest to the rescue was at September the 5th, 2008, securities lending contingency plan.

Q. And did you study AIG's analysis?
A. Yes.
Q. If you could turn to -- well, we've already moved in DX 1901. Is that right? Okay.
If we can move to the next slide, DX 2728, and what is shown here?
A. This is showing the difference between Dr. Cragg's analysis and the reality due to the constraints to engage in securities lending, loans, interaffiliate loans, by the regulatory agencies, i.e., the insurance company regulators. And the yellow line is the difference between -- or yellow bar -- the blue bar and the red bar we just saw that Dr. Cragg claims would be the excess liquidity that would be available to AIG for each of these subsidiaries.
The little green box is showing how much was actually truly available; that is, the large amount, the yellow boxes, were -- I'll just say yellow lines or bars -- were trapped in the -- in the subsidiaries, and actually, the untrapped liquidity is those small green bars. So, you can see there's a considerable difference between the trapped and untrapped liquidity. And to my mind, the relevant bar is the green bar, because this is the regulatory restrictions imposed on AIG's insurance subsidiaries.

Q. And where did the information for the green bar on this demonstrative come from?
A. It comes directly from the AIG Securities Lending contingency plan of September 2005 [sic].
MR. ROBERSON: Can I have PTX 1502 to distribute? Thank you.
May I approach?
THE COURT: Yes.
BY MR. ROBERSON:
Q. And what is this document, 1502?
A. This is the securities lending liquidity contingency plan of September the 5th, 2008, of AIG.
Q. And just to be clear for the record, a moment ago, when you said that you relied on AIG information, what was the date of the information you relied upon?
A. September the 5th, 2008.
Q. Right, okay. And it's the document we're looking at, 1502, right?
A. Correct.
Q. Okay. Now, did you make any adjustments to the analysis done by AIG that is reflected here?
A. No.
Q. Okay. If you would turn to the last -- well, let me ask you this. Turn to the last page of this document, which is, I think, internally numbered page

25 --
A. Yes.
Q. -- and the Bates number is AIG-STARR-00118828. And can you tell me -- tell me what's being set forth here?
A. It says this is the regulatory constraints I just mentioned about repo and securities lending affiliate transactions.
Q. And which column did you use to determine the amount of liquidity that AIG's insurance subsidiaries had that was not trapped?
A. The last column.
Q. Okay. It's the one called "Remaining Capacity after GSL Liquidity Transactions from 2007"?
A. That's correct.
Q. So, let's now go to your next demonstrative, DX 2729, and what is described here?
A. Well, if I added up all of the untrapped liquidity across those -- the 13 securities lending insurance subsidiaries considered by Dr. Cragg, I get $2.6 billion untrapped liquidity that could be transferred upstream to make loans within the insurance affiliates, versus his aggregate of just summing the yellow bars, which assumes there is no regulatory constraints on the affiliate transactions, and you see

it's 58.5 billion.
So, the reality is actually the ability to transfer to meet security withdrawals from the PDCF would be much less than claimed by Dr. Cragg.
MR. ROBERSON: Your Honor, we would move to admit PTX 1502 if it's not already admitted. I'm not sure.
It's already admitted? I apologize.
THE COURT: It's already in.
MR. ROBERSON: Yes.
BY MR. ROBERSON:
Q. If you could turn to your next slide. This is your primary opinion four. Can you tell us what this is?
A. This is the ex ante risk of lending to AIG was extremely high as of September 16th, 2008.
Q. And what do you mean by the term "ex ante"?
A. Ex ante is the time immediately surrounding a particular decision to make a loan.
Q. And what is the ex ante measurement date that you use in your analysis?
A. September 16th, 2008.
Q. And why did you analyze the risk of lending to AIG as of September 16th, 2008?
A. Because this is the day on which the loan was

decided to be made.

Q. How is that consistent, if at all, with how lenders make credit decisions?

A. Well, they -- they take into account all the information available to them up until that moment when they make the decision to make the loan. So, they rely on, you know, historic and current information, the most pertinent information in making a loan in terms of, you know, what is the probability of that company defaulting; what's the severity of loss if it does default.

Q. What is credit risk, Professor Saunders?

A. As I just mentioned, credit risk has two dimensions. One is -- it's called the probability of a counterparty defaulting, and the second, if it does default, what's the severity of loss, so what's the loss given default? How much is recoverable from the collateral underlying the loan?

Q. And how did you evaluate the risk of lending to AIG?

A. I looked at four characteristics on the next slide, 2731.

Q. Can you discuss those?

A. Yes. The first was AIG's financial condition was highly distressed. So, in other words, the ex ante risk of lending to AIG was extremely high. As I said, there was four factors. One was AIG's financial condition was highly distressed. There was significant uncertainty about AIG's future prospects. The type of collateral pledged to secure the loan was illiquid and nearly perfectly correlated with the likelihood of default. And the repayment of the loan was dependent upon asset sales and at a time when asset values were highly volatile.

Q. Well, let's take each of these factors one at a time, and if you would turn to slide 2732, let's discuss AIG's distressed financial condition. How did AIG's distressed financial condition affect the ex ante risk of lending to AIG?

A. I first looked at market indicators to see the degree of distress that was being reflected in the market as of the 16th of September related to AIG, and I took three indicators: One was the stock price, one was CDS spreads, and one was unsecured debt yields on AIG.

Q. And what was the date that you used to evaluate these market indicators?

A. As I mentioned, September the 16th, 2008.

Q. Okay, and let's look at the stock price. What did AIG's stock price on September 16th, 2008, indicate about AIG's financial condition?

A. The stock price, as you see, was very low. $1.85 is the price at which it opened, and two minutes later, it dropped to $1.25. The inference in finance is that, you know, the equity of a company can be viewed as a call option on the assets of that company, which simply means the more the assets are valued relative to the debt, the higher the value of equity in the company. As the asset value falls relative to its debt, then the value of the equity in the company would also fall.

So, a low stock price reflects the low equity value of that call option and, therefore, would indicate a high probability of default by AIG. So, in other words, in simple terms, a lower stock price indicates a higher probability of default, simply because the call option has got very small value.

Q. Okay. And what did AIG's CDS spreads and the yield on its unsecured debt indicate about AIG's financial condition as of September 16th, 2008?

A. Perhaps we could turn to the next demonstrative.

MR. ROBERSON: Before we do, we would like to move in, under Rule 703, DX 1924.

MR. BOIES: No objection, Your Honor.

THE COURT: Defendant's Exhibit 1924 is admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 1924 was admitted

into evidence.)

THE WITNESS: So, demonstrative 2733 shows, in the green bars, CDS spreads on AIG's debt on September 16th, 2008, the one-year CDS spread and the two-year CDS spread, and as you can see, the one-year CDS spread stood at 55.5 percent or 5550 basis points, and the two-year CDS spread was 43.3 percent or 4330 basis points, clearly extremely high, indicating a high probability of default and a loss on default if that occurred.

And on the right-hand side, you see the blue boxes, which are the yields on AIG's unsecured bonds of maturity between two and three years, and it shows the low on the date of the 16th and the high on the date of the 16th of September of 2008.

BY MR. ROBERSON:

Q. And what do the CDS spreads and yields on unsecured debt indicate about AIG's financial condition as of September 16th, 2008?

A. That it was in distress.

Q. And how would that affect the risk of lending to AIG at that point?

A. It would make it very risky to lend to a distressed firm.

Q. Now, let's move on to your next metric with respect to the risk of lending to AIG. If you would turn to slides 34 and 35, describe this, and tell us what your second metric again is.

A. The second metric is a significant uncertainty about AIG's future prospects. So, I first looked at liquidity indicators as of the -- as of September 16th, 2008, as indicative of the uncertainty about AIG's future prospects.

Q. What is the relationship between the uncertainty about future prospects and the risk of lending?

A. Well, clearly the more riskier the prospects are, the more riskier the loan, and the less liquid -- liquidity a company has, the more likely it is to default on its loan. So, that's why I looked at liquidity indicators as of September 16th, 2008.

Q. So, focusing here on slide 34, what is the first liquidity indicator that you identified in this slide?

A. Just generally, the overall uncertainty regarding AIG's liquidity needs around the time at which the loan was made, and on the 12th of September, the estimated liquidity needs were around 19 billion, but they grew to 93 billion by September 16th, as recorded in the board meeting as of that date.

Q. Why is uncertainty about the amount of AIG's liquidity needs relevant to the risk of lending to AIG?

A. As I mentioned, if you don't have liquidity, then you may not be able to cover your debts as they come due, and you're more likely to default on your debt.

Q. Now, what is the second liquidity indicator that you identified?

A. As I say, on the 16th, counterparties, particularly, were not willing to transact with AIG even on a secured basis. For example, in the repo market, counterparties were unwilling to transact.

Q. What is the third liquidity indicator that you identify?

A. On the 15th of September, we know that S&P downgraded AIG by three notches and Moody's downgraded it by two notches.

Q. And why would the downgrades affect AIG's liquidity obligations?

A. Well, first it would make securities lenders -- suppliers of collateral more reluctant to engage in securities lending transactions. It would have led to, as I discussed earlier, about collateral calls on the CDS written on the CDOs.

Also, AIG had a number of guaranteed investment contracts, or GICs, that required a collateral requirement should there be a downgrade. So, there would be severe liquidity constraints resulting from downgrades on AIG.

Q. Now, do you recall how much collateral FP estimated that it would have to post as a result of the downgrades by S&P and Moody's on September 15th, 2008?

A. Yeah. I believe it was 20 billion.

MR. ROBERSON: I'd like to move into evidence DX 426 and DX 428 under Rule 703.

MR. BOIES: No objection, Your Honor.

THE COURT: Defendant's Exhibits 426 and 428 are admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 426 was admitted into evidence.)

(Defendant's Exhibit Number 428 was admitted into evidence.)

BY MR. ROBERSON:

Q. Now, if you will move to your next slide, which is DX 2735, what is the fourth liquidity indicator that you identify?

A. This indicates that AIG, especially its leasing corporation subsidiary and its general finance subsidiary, relied on short-term commercial paper to finance its activities, and there was reluctance starting on the 12th, I believe, to roll over -- which means renew -- the commercial paper loans to AIG and its subsidiaries.

Q. What is the fifth liquidity indicator that you identify?

A. Generally speaking, when firms organize a commercial paper program, they have a backup line of credit which -- just in case they cannot roll their commercial paper, and these are very rarely used, but when they are used, it's viewed as a very negative signal.

In other words, they start to draw on their backup lines of credit for these liquidity shortfalls, and it's a very bad signal.

Q. What does that signal indicate?

A. Extreme liquidity constraints on the corporation.

Q. What is the sixth liquidity indicator that you identify?

A. There was significant redemptions in its securities lending portfolio. Most security collateral providers were reluctant to roll the securities lending collateral.

Q. When did the collateral posting requirements in the sec lending redemptions start placing stress on AIG's parent company's liquidity?

A. I believe it started even as early as September, there was concerns about securities lending collateral provisions.

Q. When you say as early as September, is there a time in September?

A. Offhand, I can't remember.

Q. Okay.

A. I remember sometime in September, before the 16th.

Q. Okay. What is the seventh liquidity indicator that you identify?

A. There was this interaffiliate loan, that insurance companies could lend under an intercompany lending agreement to AIG, and the insurance regulators are very conservative and they are worried about upstreaming to AIG when it was in such a problem. So, they stopped allowing the insurance companies to upstream funds to AIG.

Q. Through the intercompany --

A. Through the intercompany lending agreement.

MR. ROBERSON: Your Honor, we move to admit DX 1443, DX 1893, and DX 1894 under Rule 703.

MR. BOIES: Your Honor, I assume that it is the representation of counsel and the witness that all of the documents that are cited here on his charts are documents that he relied on in forming his opinions.

MR. ROBERSON: I'll let the witness speak.

THE WITNESS: Yes.

MR. BOIES: In that case, no objection, Your Honor.

THE COURT: All right. Defendant's Exhibits 1443, 1893, and 1894 are admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 1443 was admitted into evidence.)

(Defendant's Exhibit Number 1893 was admitted into evidence.)

(Defendant's Exhibit Number 1894 was admitted into evidence.)

BY MR. ROBERSON:

Q. Now, did you investigate any other measures related to the uncertainty of AIG's future prospects as of September 16th, 2008?

A. There was also uncertainty about the -- their offshore or non-U.S. insurance subsidiaries. They played a big role in AIG. I believe in 2006 they generated something like 47 percent of the total profits of AIG, whereas the domestic subsidiaries, about 53 percent. So, they played a very important role, and so I looked at the operational problems of these -- of these offshore subsidiaries as of September 16th, 2008, to see what -- what was happening there in terms of uncertainty about their liquidity needs and their solvency.

Q. And if you could turn to DX 2736, can you describe what you're setting forth in this demonstrative?

A. Well, these are a number of issues that came up on -- around the 16th regarding the activities of AIG's subsidiaries offshore. In the UK, the subsidiary there had a money market fund called PAB, and there was actually a run on the fund, and the fund was very large, about 6 billion, and AIG had to step in to freeze redemptions.

There was also -- Singapore and Hong Kong regulators issued intervention letters restricting AIG's activities, again, especially in movement of funds around AIG's entities without their approval.

Korean regulators demanded that AIG resolve the immediate capital issue, as we are below minimum solvency. In other words, they were concerned about the actual solvency of the Korean subsidiaries.

ALICO Japan had solvency issues and may be in breach.

AIA and Nan Shan solvency had deteriorated, and countries in Asia reported significant inquiries from policyholders regarding surrenders of their policies. And there was actually news reports of a run on Hong Kong operations by retail depositors.

So, this suggests that there were non-U.S. operational indicators of the uncertainty regarding the future prospects of AIG.

Q. And how would that affect the risk of lending to AIG?

A. Well, clearly, this would also -- since they played such a significant role in AIG and its profitability, going forward, this would clearly affect the probability of default and, therefore, the credit risk.

MR. ROBERSON: Your Honor, we move to admit DX 176, DX 1896, and DX 1442 under Rule 703.

MR. BOIES: No objection, Your Honor.

THE COURT: Defendant's Exhibits 176, 1896, and 1442 are admitted with a Rule 703 restriction.

(Defendant's Exhibit Number 176 was admitted into evidence.)

(Defendant's Exhibit Number 1896 was admitted into evidence.)

(Defendant's Exhibit Number 1442 was admitted into evidence.)

BY MR. ROBERSON:

Q. So, let's move on --

THE COURT: Mr. Roberson, should we take a break now?

MR. ROBERSON: Yes, Your Honor.

THE COURT: All right. We will reconvene at 11:15.

(Court in recess.)

THE COURT: Thank you. Please be seated.

Please go ahead.

MR. ROBERSON: Thank you, Your Honor.

BY MR. ROBERSON:

Q. Professor Saunders, we've been talking about your fourth opinion, the ex ante risk that loaning to AIG was extremely high as of September 16th, 2008.

A. Yes.

Q. And do you recall earlier we discussed your slide DX 2733, which is titled "AIG's Distressed Financial Condition" and it sets forth market indicators? And you discussed the yield on the unsecured debt. Those are the two blue bars on the right-hand side.

A. Yes.

Q. I don't think you put into the record, and I would just ask you to do so, what the yields on the unsecured debt was and just explain it again.

A. Yeah. For the two- to three-year traded unsecured debt, the low issue was 28.1 percent, and the high issue, 58.9 percent.

Q. And when you say low yield versus high yield, what are you referring to?

A. Well, these are bonds that traded -- some bonds traded as low as 28.1 percent yield and some 58.9 percent or in between. There's a number of bonds out there traded, so this is the low versus the high.

Q. Okay, thank you. I just wanted to clarify that.

Now, we're going to move on to your next ex ante risk metric, which involves the type of collateral pledged to secure the loan. Could you start by describing the primary type of collateral that AIG pledged to secure the credit facility?

A. These were the nontradable or nontraded liquid equity interests in its insurance subsidiaries, basically shares that AIG owned 100 percent of those insurance subsidiaries.

Q. And why did you evaluate the collateral that was pledged to secure the loan?

A. Because if things go wrong, that's -- that's the recourse of the lender to the collateral.

Q. Now, if you could turn to DX 2737, can you describe what is reflected in this demonstrative?

A. Yes. It's just discussing the type of collateral pledged to secure the loan, and the first point is the point I just made, that the type of collateral was really not tradable. It was not traded. It was the illiquid equity interests in AIG's insurance subsidiaries. So, thus, it was recognized it was not market traded; that they were illiquid.

The second is you usually want collateral to be independent of the prospects of default of a company. Here we have a case where the equity interests are pretty close to perfectly correlated with the potential default risk on the loan.

Q. And can you explain why you say there is a near perfect correlation between the value of the equity interests and the likelihood of default?

A. Well, there's two ways to think of it. If insurance companies, which is the -- are the collateral, get into trouble, then AIG would be in trouble because of the importance of the subsidiaries in providing earnings to the company, and that would suggest there's a higher probability of default; or if AIG itself got into problems, then insurance regulators would be most likely to come in and seize the insurance companies or at least place them into conservatorship to protect the policyholders.

So, basically, as AIG's subsidiaries -- insurance subsidiaries' prospects declined, that was consistent with an increase in default risk of the loan. So, basically, it's a perfect or almost perfect correlation between the risk of default on an AIG loan and the risk of default on the value of collateral underlying that loan.

Q. Okay. Now, can you provide an example of collateral that would not be nearly perfectly correlated with the likelihood of default of the borrower?

A. Oh, probably the safest collateral would be treasury bonds of the U.S. Government, because whatever happened, say, to AIG or to any company, the treasury bonds would generally have no change in value. So, they are independent or the outcome of the loan is independent of the collateral that backs up the loan.

Q. Now, given the correlation risk that you discussed, from an economic perspective, what is the AIG loan comparable to?

A. In my opinion, it's close to being an unsecured loan.

Q. Okay. And what, if anything, is the significance of the fact that the AIG loan was comparable to an unsecured loan because of the correlation risk?

A. Well, this makes then the metric of, say, the CDS spread, which is a spread or fee against a risk of an unsecured loan, relevant to thinking about the credit premium that should be charged on AIG loans.

Q. Now, let's move on to your next ex ante credit risk factor, which is the repayment source for the loan, but before we turn to the next demonstrative, how was AIG expected to repay the loan?

A. Through sale of assets.

Q. And how, if at all, did the reliance on sale of assets for repayment of the loan affect the risk of AIG?

A. Well, it was uncertain at the time on whether or if it could engage in asset sales. At the time, asset values were highly volatile, and there was a downward trend in asset values. So, there was a lot of uncertainty about, you know, the ability to actually pay off the loan through selling assets.

Q. And how did that affect the risk of the loan?

A. It clearly affected the risk of the loan if you don't know when or if the loan is going to -- going to be able to be repaid by generating value from the sale of assets, which is the main source of repayment given the fact that AIG's cash flow was so -- was so low; in fact, it was negative.

Q. Now, turn to DX 2738, and can you explain this demonstrative?

A. Well, it's indicating what I just said, and it has two comments that indicate concerns about the asset value being the source of the repayment of the loan. And I think the first one originated, I think, from Mr. Lee, who was basically explaining why the syndicated loan couldn't take place because of concerns about the ability to realize enough value from assets to cover the syndicated loan. And it says the "hole was too big to be filled..." I think it was repeated by Kevin Warsh in a memo to the Fed.

And the second one is actually based on handwritten notes of Margaret McConnell, who was in a meeting at the Fed, at the Federal Reserve Bank of New York, and it was basically that there was significant risk that you won't recover principal and interest on this loan. So, basically the problem or the issue was when or if could you sell assets and at what price.

Q. Did AIG and the New York Fed need time for asset sales -- asset values to recover in order for AIG to be able to repay the loan?

A. Yes.

Q. And what was happening to asset values in general around this time?

A. As I said, asset values had been trending down, but there was a lot of volatility around that trend. There was a great deal of uncertainty about the value of assets as of that time.

Q. And what is the significance of the volatility in asset values with respect to credit risk?

A. Well, it increases the risk of the loan, because it's hard to evaluate the underlying assets' values that were backing the loan.

Q. Now, what concerns, if any, were expressed by the New York Fed as of September 16th, 2008, about the possibility of sustaining a loss on a loan to AIG?

A. Well, I think I just mentioned the two comments, (a) and (b), that were made at the time at the Fed about concerns about the risk of the loan in terms of the asset sale as a source of revenue to repay the loan.

MR. ROBERSON: Your Honor, we would move to admit DX 363, DX 976, and DX 375 under Rule 703.

MR. BOIES: No objection with that limitation, Your Honor.

THE COURT: All right. Defendant's Exhibits 363, 976, and 375 are admitted with a Rule 703 limitation.

(Defendant's Exhibit Number 363 was admitted into evidence.)

(Defendant's Exhibit Number 976 was admitted

into evidence.)

(Defendant's Exhibit Number 375 was admitted into evidence.)

BY MR. ROBERSON:

Q. Now, can you turn to the next slide, Professor Saunders.

A. Yes.

Q. And can you tell us what your fifth primary opinion is?

A. The rescue transaction did not result in an economic loss to the credit agreement class.

Q. And if you would turn to your next slide, what is the purpose of this demonstrative?

A. Just to explain that an ownership interest dilution, such as occurred in this case, does not necessarily result in economic dilution or loss. There's a distinction between ownership dilution and economic dilution.

Q. Can you explain that distinction?

A. Simply the -- your ownership share might be diluted, in other words, you might be diluted down to partial ownership share, but the value of those shares could go up. There's not necessarily any reason why the market value of the shares you own would actually fall as well. They are distinct.

Q. And what do you mean by "economic dilution"?

A. A fall in the value of the shares that you own -- that you're owning as part of your ownership interest. So, if the original shareholders were diluted but the value of those shares go up, then ownership interest dilution is different from economic dilution or loss.

Q. Now, why doesn't ownership interest dilution always cause economic dilution?

A. I've prepared a couple of hypotheticals just to try to explain why.

Q. Okay. If you could turn to your next slide, DX 2741, what are you setting out in the title of this demonstrative?

A. This is showing the issuance of shares to new shareholders in exchange for reasonably equivalent value will cause ownership interest dilution but not an economic loss.

Q. And can you walk us through the example shown in this demonstrative?

A. This is looking at a situation before and after a transaction takes place, dilutes ownership interest -- results in ownership interest dilution of the original shareholders but does not result in economic dilution, just to make the point that ownership dilution is different from economic dilution.

And this is a -- this is a hypothetical I conceived to try to explain as easy as I can the difference between the two. So, looking at row A, this is before any ownership dilution, and I'm assuming the original shareholders own a billion shares and it's worth, fair value, $10 a share. So, their ownership percentage is 100, and one billion times $10 per share is 10 billion. So, their economic interest or their economic value is 10 billion for their shares.

And row B, a transaction takes place where new shareholders come in and receive 4 billion shares, and -- but they do pay the fair value. They pay $10 a share. They now own 80 percent of the company, but the value of the company has increased by 40 billion, because the 4 billion new shareholders are paying $10 a share each.

So, the final outcome is the after row, row C. The original shareholders still own 1 billion shares at a price of $10 a share. They only own 20 percent, because they've been diluted down from 100 percent to 20 percent in terms of ownership, but the value of the company has grown to 50 billion, because there's 40 billion extra equity value added by the new shareholders.

So, overall, the total equity value after the transaction is 50 billion in the company, 10 plus 40 gives you 50 billion, and the ownership stake of the original shareholders had been diluted to 20 percent, but the value of their claim, 20 percent of 50 billion, is 10 billion.

So, the final conclusion at the bottom is that even though the original shareholders' owned percentage -- ownership percentages diluted to 20 percent, they suffered no economic loss. So, you see the zero dollars in the bottom right-hand corner of the demonstrative.

Q. Okay. And if you could turn to your next example of dilution, to 2742, DX 2742, can you walk us through this slide and tell us what you're trying to set out in this slide.

A. Again, it's a hypothetical but to try to make the point that ownership interest dilution and economic dilution can only occur when new shares are issued in a transaction for less than reasonably equivalent value. So, it's a similar transaction, but there's one big difference, as I'll get to in a minute.

So, row A is the before position, where the original shareholders own 1 billion shares at a price of $10 a share. They own 100 percent of the company, and the value of the equity of the company is 10 billion. So, their shareholders -- their economic interest is 10 billion. Excuse me.

A new transaction takes place, which is row B. Some new shareholders come in, and they take 4 billion shares in the company, but they do not pay anything, zero. So, there's no price paid for those 4 billion shares. So, their ownership percent is now 80 percent, but they have not increased the value of the company at all because they've paid zero for the 4 billion shares. So, the red box is showing zero increase in equity value.

The last row, row C, shows after the transaction, where the original shareholders still own a billion shares but now at a price of $2 a share, because there's been no increase in the value of the equity of the company, and the total shareholders' equity interest has declined from 10 billion to 2 billion. So, these new shareholders who paid nothing really diluted down both ownership dilution and economic dilution, the value of the shares of the company.

And the conclusion at the bottom is that in this hypothetical where nothing is paid -- this extreme hypothetical where nothing is paid for the value of the shares, the ownership shareholder percentage is diluted

20 percent, and they do suffer an economic loss. And in this case, the value of their -- their share value falls from 10 billion to 2 billion, and they lose, therefore, 8 billion, which is the bottom right-hand corner of the demonstrative.

Q. Would there be economic dilution if the new shareholders simply took possession of the existing shareholders' shares without compensation rather than receiving new shares?

A. Yes. It's basically the same thing, and the original shareholders would be diluted down to 20 percent, and their share ownership value would be, again, 2 billion. So, it would basically be the same thing.

Q. Now, in each of the two examples that you've just marched us through, you do a before and after comparison.

A. Yes.

Q. And why is that?

A. Because I think it's the correct way to think about it, what was the value the original shareholders claimed before, the ownership dilution, what happened to the economic value after the ownership dilution. So, I call it the before and after framework, a way to think about it, what happened to the original shareholders before, what happened to them afterwards, and did the value of their shares, the total value, equity value, did it increase or decrease or stay the same.

And it's quite possible all three things could occur, either you increase economic value or you decrease economic value, no change, even though you have had ownership dilution. So, the distinction I'm trying to make is between ownership dilution and economic dilution.

Q. Okay. Let's start with the value of AIG's equity prior to the ownership interest dilution, and if you could turn to the next slide, what does this slide illustrate?

A. Well, it's just repeating what I just said. The correct framework for analyzing economic dilution requires a calculation of the value of AIG's common equity prior to and after the ownership interest dilution.

Q. Okay. Now, if you turn to the next slide, DX 2744, what does this demonstrative illustrate?

A. This is based on the opening price of September the 16th times the number of original shares out there, and 100 percent ownership claim by those original shareholders was worth $5 billion, which is the blue bar or blue box at the bottom of the graph.

Q. Now, what would you expect to happen to the $5 billion value of existing shareholders' shares if no value was provided for the 79.9 percent equity interest?

A. It would decline.

Q. Okay. And why did you use the opening value on September 16th as the starting point for your before and after comparison?

A. As I explain a bit more a bit later on, what I have used is the clean price, the clean before price, before a rescue transaction took place. I think over the day after the CNN -- CNBC news broadcast, around 10:50 on the morning of the 16th, expectations grew as to a possible rescue, whereas at the opening, the news was all bad about the impending potential bankruptcy of AIG. So, I view this as the clean, you know, pre-rescue price to evaluate what happened to -- before and after the ownership dilution.

Q. And what did happen to the value of AIG's shares -- shareholders' shares after the rescue?

A. If we could look at the next demonstrative, 2745.

Q. Okay.

A. And the left-hand box, this was in a prior slide, was the 5 billion value as of the opening price on the 16th, and on the right-hand side is the value of the shares of AIG using the 17th opening price. I used this because the rescue was announced on the evening of the 16th, and funds were provided on the 16th in the evening, and the market became aware of that overnight. In an efficient market, the stock price should reflect all available information immediately. The opening price is the correct metric to look at this.

And there's -- you can see that the -- first of all, the area A, which is the original shareholders' stake, has grown from 5 billion, an extra 1.2 billion, to 6.2 billion, because the stock price rose from the 16th, it opened at $1.85, and on the 17th, it was $2.29. So, clearly the stock price rose, and, therefore, the original shareholders, if you held the same number of shares, that value increased and it increased from 5 billion to 6.2 billion. And that's indicated in the black box there, that shareholders did not lose value, but rather gained an extra $1.2 billion. So, this is, again, showing ownership dilution does not result in economic dilution. In other words, in this case at hand, the ownership dilution did not lead to economic dilution for the original shareholders.

Q. What is the green bar on this chart?

A. This is the extra value created as a result of the rescue and the 79.9 percent equity provision as part of the rescue, and it's the new number of shares that were issued, the 11.6 billion extra shares, times $2.29, and it gives you an extra 26.7 billion in value -- equity value to AIG.

So, the total value of the rescue, in terms of -- including new shares and the additional value of the old shares, is the sum of the blue hatched area, which is 1.2 billion, which is the extra gain of the original shareholders, plus the extra 26.7 resulting from the new shareholders' equity provision, and in the red box, as it says here, "The $27.9 billion increase reflects the value received by AIG in exchange for the rescue." So, it's the area C, the sum of the 1.2 billion cross-hatched area, blue cross-hatched area, and the 26.7 green box area.

So, in net, the basic point is just to show that in this case, ownership dilution did not lead to economic dilution for the original shareholders; in fact, they benefited.

Q. If no value was provided to AIG in exchange for the shares, how could AIG's market value have increased by $27.9 billion on September 17th, 2008?

A. It couldn't have.

Q. Why not?

A. Because value was provided. If no value was provided, the $5 billion box would shrink, would shrink in size, because nobody would provide it. Then some ownership stake would be taken in the company with no provision of value; therefore, the original owners would be downsized in terms of the value of the ownership of the company.

Q. If you turn to the next slide, is that what you're describing?

A. Yes. The next slide shows a hypothetical case where no value was provided. If no value was provided by the new shareholders, therefore, there's no increase in value over the 5 billion beforehand. And you can see the effect of an 80 percent equity interest being taken by a new equityholder without any value created or any value provided. So, what's left then is the 20 percent remaining original shareholders, their stake has been diluted from 5 billion down to 1 billion, and 4 billion is now owned by the new equity owners, even though it didn't pay anything for the shares.

Q. Now, did you investigate the change in AIG's market value between the opening on September 16th, 2008, and another date other than the 17th of September?

A. Yes. I also looked at the date Dr. Kothari picked as the date at which the credit agreement signing was known to the market. He takes the close of the 24th as being a relevant date in his -- in his assessment.

Q. If you would turn to slide DX 2747, and what's illustrated here?

A. This just shows the same sort of type of calculation, but I'm using now the closing price on the 24th in the far right box, which was higher, $3.31, than the $2.29 on the 17th opening. As you can see, the original shareholders' value, which was 5 billion in the before situation, before the rescue transaction, increased after the rescue transaction by 3.9 billion.

In other words, because the price -- stock price was $1.85 on the 16th, then $3.31 at the close on the 24th, the value of the original shareholders' claims increased by 3.9 billion. So, in total, their shareholdings were now worth 8.9 billion, and that, in terms of percentages, is almost an 80 percent increase in their value. So, it's hard to see how you could claim that that's economic dilution. In fact, they did very well. They made an 80 percent increase in their value as of the 24th of December -- of September, 2008.

Q. Can you explain the green bar and the hashed bars together? What do those sort of represent?

A. Again, the green -- the hashed bars, as I said, reflects the additional equity value of the original shareholders, 3.9 in additional value, because the price is higher on the 24th than the 16th, and the original shareholders still held the same number of shares.

And the green box is the additional value provided to AIG as a result of the rescue, which results in an extra 11.6 billion shares times the new price, $3.31, which produces an extra value of $38.7 billion.

So, in total, as shown in the red box, there's a $42.6 billion increase in the value received by AIG in exchange for the rescue. Part was provided to the old shareholders, 3.9, and part is reflected in an increase in AIG value of 38.7 because of the contribution of the rescue reflected in the 38.7 billion green box.

Q. Can you provide us some examples of the types of value that the rescue created for AIG and its existing shareholders?

A. If we can turn to the next demonstrative, 2748, this is three sources of value that was created as a result of the rescue that's being reflected in the equity value of the company after the transaction, after the rescue transaction, and in brief, first of all, A, it allowed AIG to continue as a going concern.

Q. And what do you mean by your phrase "AIG was able to continue as a going-concern"?

A. Well, because of the liquidity provision, it was able or better able to pay its debts as they came due.

I think a going concern company is a company able to pay its debts as they come due. If it can't pay its debt as it comes due, then clearly there's a going concern opinion by the auditors against the company, and that has serious external effects in terms of its ability to attract customers and its reputation, et cetera. And implicitly, it's close to bankruptcy.

Q. And what's the second value that you set forth here?

A. It received the funding at below-market financing in the sense that it's -- the interest rate on the loan, LIBOR plus 8 1/2 percent, was below the CDS spread as of the time, or one way to think of it, the 8 1/2 percent credit premium on the loan was below the CDS spread, which, as I mentioned, reflects the unsecured premium on a -- on an unsecured loan.

So, as I mentioned, with the collateral being mostly illiquid, nontraded equity interest in the subsidiaries, the collateral was similar or the loan was similar to an uncollateralized loan, so it makes the metric of comparing the CDS spread with the 8 1/2 percent relevant, and clearly the 8 1/2 percent was lower than the CDS spread as of the 16th and virtually any time during September.

Q. And what was the other metric in terms of market financing that AIG experienced that we began discussing that after this break?

A. In terms of number C here?

Q. No, in terms of B.

A. Well, B, because we -- as I showed, as -- the CDS spread was extremely high. It was -- it was 55 percent, if I remember, for the one-year CDS and around 43 percent for the two-year CDS, and the credit premium on the loan itself was 8 1/2 percent. So, clearly there's a big discrepancy between what the free market viewed as the appropriate credit premium rate and what the -- what the Fed charged in terms of providing the financing.

Q. And how did the Fed financing compare to the yields of unsecured debt?

A. Again, if you remember the blue box we discussed, the minimum yield on traded unsecured debt out there on that day on which the loan was provided was around 26, 27 -- I'm trying to remember the numbers, around 26, 27 percent, with a high around 50 percent.

Q. Okay. And what was the -- what's the third --

A. The third is the -- you know, if the rescue hadn't been provided, there's a high probability that AIG would have been forced into bankruptcy, and there are very large -- well, something called direct and indirect costs of bankruptcy.

Q. Can you describe what a direct cost of bankruptcy is?

A. Direct costs are more easily measurable and would involve legal fees, for example, accounting fees, direct restructuring fees that one can measure, and the academic literature has done a lot of studies on this, and it's estimated that, roughly, the direct costs of bankruptcy are at around 3 percent to 6 percent of firm value.

Q. What do you mean by indirect costs of bankruptcy?

A. These are much more harder to measure, because if a company goes bankrupt, its customers switch away, management moves on, you lose most of your best talent. So, people have tried to measure this, and there are a number of papers out there. There's quite a range of values, generally between -- from the papers I've seen, between 10 percent and 30 percent of firm value is lost due to these reputational losses and switching by customers away from the company. So, you know, the indirect costs are generally viewed as being larger than the direct costs, but both are significant in terms of loss of firm value.

Q. Now, did the benefits of the rescue you identify in this demonstrative also extend to AIG's existing shareholders?

A. Yes.

Q. And how so?

A. Because they -- they gained from the rescue.

Q. In terms of the stock price?

A. Yes. As I mentioned earlier, they -- they -- the stock price rose, and they gained in value.

Q. So, let's change from market value to stock price. If you would turn to slide 2749.

A. This just says that another way to think about whether the original shareholders suffered an economic loss is by looking at the share prices, and if there was ownership dilution, then after the dilution, the stock price would be lower, basically, which is sort of another way to -- another lens to view the distinction between ownership dilution and economic dilution.

So, in terms of stock price, ownership dilution could lead into either a higher stock price, the same stock price, or a lower stock price. If the stock price fell after an ownership dilution, that would be consistent with an economic dilution.

Q. Okay. If you could turn to the next slide, what are you setting forth in this slide?

A. This is just showing the prices on September

16th, 2008, showing the opening price at 9:30 a.m., when the market was $1.85, and it fell two minutes later, at 9:32, to $1.25, and that clearly is a pre-rescue value, because at the time there was very, very -- if you looked at a Newswire, there was a lot of suggestions that AIG may well file for bankruptcy soon.

And then at 10:52, CNBC came out with this news item discussing the expectation of a rescue, and that seemed to develop over the day. So, the closing price at 4:00 p.m. was $3.75. So, I've used that price reflecting the expectation -- an expectation of a rescue, whereas the $1.85, to my mind, reflects the pre-rescue value before and when it's really felt that there was a high probability that AIG would go bankrupt.

Q. So, let's look at what happened to AIG's stock price after September 16th, 2008. If you could turn to slide 2751, what are you setting out in the title of this demonstrative?

A. This is showing over the whole period, from the opening price on the 16th to the closing price on the 24th, the share prices on either the opening or the close on each of those days, and you can see the pre-rescue price at -- and I'm taking the opening of $1.85, and I could take the intraday low, $1.25, because that was just two minutes later, but just comparing the

$1.85 with the prices on opening and close that followed, right up to the 24th, which the yellow boxes are the opening prices on each of those days up to the 24th, and the blue bars are the closing prices.

On no day did any of those prices fall below $1.85, or just to say conversely, the prices on each of those days -- each of those points in time, either open or close on each of those days, was above $1.85. So, obviously, a higher stock price suggests -- after a transaction suggests that the ownership dilution did not result in economic dilution. It, in fact, resulted in an economic gain.

MR. ROBERSON: Your Honor, we would move to admit DX 550.

MR. BOIES: For a limited 703 purpose?

MR. ROBERSON: Of course.

MR. BOIES: Yes. No objection, Your Honor.

THE COURT: Defendant's Exhibit 550 is admitted with a Rule 703 limitation.

(Defendant's Exhibit Number 550 was admitted into evidence.)

BY MR. ROBERSON:

Q. Now, Dr. Saunders, could you move to your next primary opinion, number six?

A. This is that Dr. Kothari's conclusion that the value of the credit agreement class claim is $35.4 billion, or in terms of shares, $13.16 per share, makes no economic sense.

Q. Let's turn to slide 53, and what are you setting forth in -- as a conclusion in this demonstrative?

A. AIG's stock price did not approach the value Dr. Kothari claims was lost under his "bounce-back" theory. So, Dr. Kothari's bounce-back theory is that the liquidity problems of AIG were temporary and that once the liquidity had been provided without the equity stake, the price on the credit agreement revelation date, which he takes to be the close of the 24th, would have bounced back to its price on the 11th, which he views as being the day before there was this -- this liquidity crisis.

So, basically his argument, the bounce-back theory, is that, A, the liquidity crisis was temporary; B, the relevant metric would be the price on the 17th -- on the 11th, excuse me. So, he comes up then with an actual value of $13.16 per share, added to the actual price, which was $3.31 per share on the 24th, to argue that the value of the shares should have been, to the original shareholders, $16.47.

Q. Can you explain how shareholders could have lost $13.16 in value per share when the opening price on

September 16th, 2008, was $1.85 per share?

A. I don't think it's possible economically.

Q. Why is that?

A. Well, it's impossible to lose more than you have in the first place.

Q. Was there any point between September 16th, 2008, and September 24th, 2008, when AIG's stock price was near $13.16?

A. No. As you can see, the -- the highest intraday price of that whole period was $5.70, which is the black box just before the closing price on the 24th bar or box, shown as having a value of $16.47.

Q. Did you review Dr. Kothari's testimony in this matter?

A. Yes.

Q. Do you recall his testimony that AIG's stock price on September 16th, 2008, did not reflect its intrinsic value?

A. Yes.

Q. And do you agree with Dr. Kothari's opinion about AIG's stock price not reflecting its intrinsic value on September 16th, 2008?

A. No, I don't. I think the stock price is an efficient statistic, and it reflects the information at the time, and it reflects the opinions of the millions of investors in the company about the firm going forward, including its liquidity position.

So, I think the relevant metric on the 16th was $1.85, based on the -- and that in the investors' belief about the intrinsic value of the firm. So, what I'm saying is that the share price reflects the intrinsic value of the firm, and on the 16th, the intrinsic value of the firm was $1.85.

Q. Under Dr. Kothari's theory, what would have happened to AIG's stock price once its immediate liquidity needs would have been resolved?

A. Well, the liquidity provision, in my opinion, was announced on the evening of the 16th, and funds started flowing out on the evening of the 16th. So, I would look at the price on the morning of the 17th, which is $2.29, as reflecting the value that was obtained from the liquidity provision.

Q. And if Dr. Kothari is correct that AIG's stock price should have bounced back once its immediate liquidity needs were resolved, on what date would the bounce-back have occurred?

A. Well, on the 17th, after the rescue was announced.

Q. And did the markets reflect any movement on the 17th?

A. On the 17th, yes, it rose from $1.85 on the opening of the 16th to $2.29 on the opening of the 17th, after -- on the opening of September 17th, after the amounts from the rescue transaction on the evening of the 16th.

Q. Did AIG's stock price bounce back on September 17th to its September 11th, 2008, price?

A. No. You see that $2.29 is below the price on September the 11th, which I think was around $17.

Q. If the credit facility had not been provided to AIG, how, if at all, would that affect Dr. Kothari's bounce-back theory?

A. If the credit -- I'm sorry, could you repeat the question?

Q. If the credit facility had not been provided to AIG, how, if at all, would that affect Dr. Kothari's bounce-back theory?

A. Well, then, it's highly likely the company would have entered bankruptcy.

Q. Now, if you could turn to the next slide, 2754, what is the purpose of this slide?

A. It's just a -- Dr. Kothari improperly treats the economic benefits or consideration received from the rescue in exchange for new shares as a proxy for the economic value lost, rather than economic value gained.

Q. What's wrong with that?
A. As I say, the value -- if the value of the shares goes up, it must be an economic value gain, not an economic value lost.
Q. And if you turn to slide DX 2755, what are you setting out as your conclusion in this slide?
A. Dr. Kothari contradictorily claims that no value was received from the new shares, even though AIG's market value increased.
Q. And can you explain why there's a contradiction in his analysis?
A. Well, I'm using -- looking at before and after. Before the transaction, the value of AIG's shares was 5 billion, as I mentioned, on the 16th, using the opening price, and once AIG had secured liquidity through the rescue transaction, if you take the date -- the revelation to the market as the closing on the 24th of September, 2008, the value of AIG's equity had risen to 44.3 billion.
Q. Now, just to make sure I understand, how much value does Dr. Kothari claim AIG received in exchange for the Series C preferred stock?
A. As I understand it, he claims only the 500 -- half a -- 500 million or half a billion loan forgiveness as part of the rescue plan was actually paid. So, in

other words, he views the benefit being received to net out against the loss as being a half a billion dollars, which was -- he claims to be the value paid by the -- the preferred C shareholders.

Q. And what does Dr. Kothari claim AIG's market value was on September 24th, 2008?

A. Forty-four billion.

Q. And what was AIG's total market value as of the opening on September 16th, 2008?

A. Five billion.

Q. A moment ago, you mentioned the consideration that Dr. Kothari claims that AIG received in exchange for the equity interests.

A. Yes.

Q. Do you recall the figure that you used when you testified a moment ago?

A. I think it was 500 million or half a billion.

Q. Are you certain of that, sir?

A. That's what I seem to remember. I might be wrong.

MR. BOIES: I have no objection if counsel wants to suggest to him another number.

BY MR. ROBERSON:

Q. $500,000?

A. Oh, 500,000, sorry. Even less than I thought.

THE COURT: Just a few zeros?

THE WITNESS: Yeah.

BY MR. ROBERSON:

Q. Now, how could -- well, I just asked you, AIG's opening value on the 16th was approximately how much?

A. Five billion.

Q. And how could AIG's market value have increased by $39 billion if the Government only provided $500,000 in value for the Series C preferred stock?

A. As I say, I don't think it's possible.

Q. Why is that?

A. It is showing that there was a considerable value gain of 44 billion, minus 5 billion, or 39 billion. It's hard to get a 39 billion gain and call it a loss. This is a value gain, not a value loss.

Q. Now, if no credit facility was provided to AIG, then would AIG's market value have increased to what Dr. Kothari claims?

A. No. It would probably have entered bankruptcy.

Q. Now, if you could turn to your next primary opinion, seven, and can you tell us what your opinion here is?

A. The opinion here is the increase in the number of unissued authorized shares did not result in an economic loss to the stock split class as of June 30, 2009.

Q. And can you turn to DX 2757. And what conclusion are you setting forth here?

A. An increase in the number of unissued authorized shares does not cause an economic loss.

Q. And can you explain why that is?

A. Well, first of all, there were no new shares issued on June 30, 2009. All that happened, there was this reverse stock split, so AIG's existing shareholders had the same percentage ownership interest before and after the reverse stock split.

So, in other words, all that happened was the number of unissued authorized shares increased, but the ownership stake of the original shareholders remained at 20 percent, 20.1 percent.

Q. And can you turn to the next slide, DX 2758, and can you tell us what this demonstrative illustrates?

A. This is from a -- generally reflects the proxy conclusion as to why or claim as to why the reverse stock split was necessary, and which it was voted on, and the major point that was made was that a delisting would have resulted in a significant loss of value for shareholders. And as I say in that first bullet point, the primary purpose of the reverse stock split was to increase the share price to avoid a delisting and to increase the purchase of AIG stock by institutional and other investors.

Q. And what does your second bullet point address?

A. An involuntary delisting results in significant loss of value to shareholders.

Q. And can you explain more about that?

A. Well, usually -- the stock was traded on the New York Stock Exchange, and I think for a while they'd stopped adhering to their minimum price rules, but they were imminently about to be removed in terms of whether a company would be delisted or not use the minimum price. And there was concern that if the NYSE reintroduced its decision to delist low-priced stock, AIG would be delisted, and if it was delisted, it would end up in what's called the pink sheets.

The pink sheets are just the over-the-counter market, which is traded between individuals who want to buy generally distressed stock, and it would trade at a very high discount to a -- say, a listed share of the same company.

Q. And have you seen academic literature that addresses the consequence of such a delisting?

A. Well, there are -- there are at least three, to my knowledge. The one that gives the most concrete number, I think, is a paper by Angel and his co-authors in the Journal of Finance in 2004, where, if I remember, he shows that the value loss of a delisting to the shareholders, by ending up on the pink sheets, is about 19 percent of equity value. So, basically, there's a huge hit to equity value if you are put down onto the pink sheets.

Q. And what are you describing in your third bullet point here?

A. Well, I think shareholders recognize that, and the third bullet point just notes that a majority of the existing common stock shareholders, including Starr itself, voted in favor of the reverse stock split. So, my view is that this is indicating that they knew about the potential disaster of a delisting and, therefore, voted in favor of the reverse stock split.

MR. ROBERSON: Your Honor, we would move to admit DX 894 under Rule 703.

MR. BOIES: No objection, Your Honor.

THE COURT: Defendant's Exhibit 894 is admitted, with a Rule 703 restriction.

(Defendant's Exhibit Number 894 was admitted into evidence.)

BY MR. ROBERSON:

Q. Professor Saunders, could you move on to your primary opinion number eight in your next slide, DX 2759.

A. That Dr. Kothari's valuation of the stock split class claim as of June 30, 2009, makes no economic sense.

Q. And you reference Dr. Kothari's valuation of the stock split class. What do you understand his valuation methodology to be?

A. If you turn to the next slide, I have an overview on 2760, the next demonstrative. I have a general overview of his stock split class claim, and his stock split class claim comes from the exchange of preferred C, E, and F claims for common stock, and his claim comes to $4.67 billion. And he divides the -- the claim into two components, a Series C claim and a Series E and F claim.

The Series C claim, as you see in the middle row, is $339 million of the total $4.6 billion -- 67 billion, and this is his claim that since Series C are more illiquid than common stock, in order to do the exchange, the Series C shareholders would have to pay a liquidity premium to the common shareholders to be able to exchange their stock from preferred -- less liquid preferred, as he claims, than a more liquid common stock.

And he applies, if I remember correctly, a liquidity premium of 5 percent, which he nets out after a bargaining agreement to 339 million. So, basically, this reflects an illiquidity cost to the common shareholders of allowing Series C shareholders to exchange without compensation. So, the 339 million is how much compensation they would expect or demand to allow the Series C to exchange into common stock.

The Series E and F claim is related to the difference between the fair value of the shares and the value of the shares that they actually received, and the claim is that the fair value of the shares was less than the value which they received on the exchange, and that amounts to $4.33 billion.

Q. And if you could turn to your next slide, DX 2761, what are you setting forth here?

A. Well, it's just a basic overview, that the total stock split class claim is flawed for the simple reason that 4.67 billion value of voting rights of the stock split class that was -- he claims was lost exceeds the value of the shareholders' common stock value of 3.58 billion on June 29th, 2009, so -- even though, actually, the 3.58 billion value includes both voting and economic rights.

So, the claim is a loss of 4.67 billion in terms of voting value, and the share has both voting value and economic value, and he claims that just a loss of the voting value alone was 4.67 billion, as a result of the reverse stock split, but the actual value of shares of AIG on June 29th, 2009, was three dollars and -- 3.58 billion, sorry, and that includes both voting and economic rights. So, it's a sum of the two.

Q. And what conclusion do you reach on --

A. Well, that's not possible. You can't lose more, again, than you -- than the value was originally, which was 3.58 billion, and only some subset of that 3.58 billion would have been voting rights anyway, because part of that would also have reflected economic rights.

Q. Okay. Let's go on and discuss your analysis of Dr. Kothari's Series C preferred stock split claim of $239 million. Did you investigate what, if any, options the Government had available to it to monetize the Series C, other than converting or exchanging it for common stock?

A. Yes, I did. It had alternatives to exchanging the Series C preferred into -- directly into common.

Q. And if you would turn to your next slide, DX 2762, what's the purpose of this slide?

A. They had at least two options, and the first I describe is what's called a depository shares option, and under the depository shares option, actually, the trust -- upon request, the trust -- AIG was obligated to enter into a depository arrangement where the Series C preferred stock shares would be deposited with a depository, and depository shares would be issued in denominations specified by the trust.

Q. Okay. Just to be sure, I think we've sort of jumped. We're -- you're now looking at 2763. Is that right?

A. Yes, I was going on to -- sorry, I should have mentioned, I was trying to explain the potential ways in which you could monetize --

Q. So, 2762, you're saying the trust had options available to it to monetize.

A. And 2763 is to start on what of those options were, and I just described that option. Basically, the idea is you got preferred stock, and the trust could deposit that preferred stock with a depository, like Mellon Bank, and then issue common shares, called ADRs, American depository receipts, backed by the cash flows from the preferred shares. And it's fairly common to do this. Many -- you know, generally it's done -- historically has been done by firms in foreign countries that want to get access to the U.S. market. They place their shares into a depository, usually Mellon Bank or -- and then Mellon Bank issues the ADR and it trades on the New York Stock Exchange.

In more recent years, actually, a number of banks have used this option. Bank of America, Citibank, Wells Fargo, among others, have taken their preferred stock, posted it as collateral with a depository, and had ADRs issued backed by those preferred shares, and they trade in the market. It's what's called ADRs, American depository receipts.

And the important thing to note is that if the trust had made this request, it did not require a shareholder vote. So, point (ii) at the bottom of box A is that the option did not require a shareholder vote.

Q. Okay. If you could turn to your next slide, DX 2764. Can you describe this second option that you've set forth?

A. The second option says the trust could have monetized the Series C shares without a shareholder vote, and I call this the trust's preferred share option. So, this is a second way in which they could have monetized the preferred stock other than doing the exchange, and, therefore, suffering the hypothetical liquidity discount that Dr. Kothari claims.

Basically, the first step to do this would be to redenominate the Series C preferred shares into smaller par values, and keeping the ratio of four to one and the original shares -- common shares were about 2.68 billion, they could redenominate the Series C preferred shares into a total number of 10.7 billion.

The net result of this would be that 80 percent of the float of shares of -- of tradable shares of AIG would be these preferred shares that have been redenominated, and then they could request that the 10.7 billion shares could be registered for sale into the public markets, and the trust could request AIG to register the shares for sale.

And then if they did so, there would be larger volume or larger float than the existing common shares, and this actually caused a lot of concern with the AIG board -- at one AIG board meeting, because there was concern that -- excuse me -- there was a concern that liquidity could flow away from the common shares into these preferred shares, so that common stock could trade at a discount relative to the preferred shares, because the preferred shares, in volume, would be much bigger than the common shares.

So, this would be with a direct way to monetize these shares. You redenominate them, you register them, and you sell them to the public.

And, again, point (iv), the important thing about this option, just like the first option, it does not require a shareholder vote of the common shareholders. So, a second way in which they could have done this was this trust preferred share option.

Q. Now, with respect to either of the two options you've described, are you aware of any steps the common shareholders could have taken to block the trust's ability to use either one of these options to monetize the Series C?

MR. BOIES: Objection to the extent it calls for a legal conclusion, Your Honor.

THE COURT: We will take your understanding on this.

THE WITNESS: Okay. Thank you, Your Honor.

My understanding is it didn't require a shareholder vote.

BY MR. ROBERSON:

Q. My question was whether they could have blocked the trust's ability to use either of these options.

A. Well, if they can't vote, I'm not quite sure how they can block them.

Q. Okay. So, let's move on and discuss your evaluation of Dr. Kothari's Series E and F preferred stock split claim, the $4.3 billion. First, do you agree with Dr. Kothari's analysis of this claim?

A. No, I don't.

Q. I'm sorry.
I've been alerted that I need to move into evidence, on 2764, DX 1898, under Rule 703.
MR. BOIES: No objection, Your Honor.
THE COURT: Defendant's Exhibit 18 -- 98 did you say?
MR. ROBERSON: 1898.
THE COURT: 1898 is admitted with a Rule 703 restriction.
(Defendant's Exhibit Number 1898 was admitted into evidence.)
BY MR. ROBERSON:
Q. Okay. So, I've just asked you whether you agreed with Dr. Kothari's analysis of the Series E and F stock split claim, and can you tell us what your opinion is on that?
A. Well, if the stock split class claim existed, it would be on June 30, 2009, but he takes a later date as the exchange for the -- calculating the loss to the Series E and F preferred stock. So, just to read the box, chronologically, the ownership and economic interests of the stock split class could not be diluted on June 30, 2009, by an exchange of the Series E and F preferred stock for common stock that occurred on June 14, 2011. In other words, is timing consistent? How

could shareholders in 2009, in June, lose by an exchange 1 1/2 years later, sitting at June 30, 2009? So, is timing consistent doesn't make chronologic sense to me.

Q. Does it make any economic sense?

A. No.

Q. Why not?

A. Well, because there's a number of things that happened between -- you know, the markets changed. Just looking at the stock price alone -- the stock price alone of AIG, I think AIG's stock was trading around $18, $19 at the end of June, and it was trading around $40 on January the 14th, 2011. So, the stock price more than doubled over this period of time. So, it was a very different market, you know, in January 2011. The value of AIG's shares was much higher than on June 30th, 2009.

Q. What is the significance, if anything, of the fact that the price of AIG's common stock had doubled?

A. Well, again, you know, if you take -- if you took the price of $40 and you converted the 47 million into common stock and you tracked it back to June 30, the value of that common stock would be much less; in other words, the number of shares you would receive. In fact, I think, if I remember, the exchange occurred at $45 a share, which was higher than the market price.

So, the number of shares received was around I think a billion dollars -- a billion in size, sorry. If you track it back to June 30, 2009, $18 a share times a billion is about 18 billion. So, there's a complete difference in value between the shares in two thousand -- on January 14th, 2011, and June 30, 2009. So, it's a bit like apples and oranges.

The value had changed considerably, and the value would be very different between those two dates for the same number of shares. So, for every share I gave you in 2009, if you valued it at that time, it would be worth much less than it would be on June -- January 14th, 2011.

Q. And what, if any, other circumstances changed between the time of the reverse stock split and January of 2011?

A. If you would turn to the next demonstrative, 2766, this is actually just -- this is making the point or I think just reiterating the point I just made, that assuming the exchange of the Series E and F caused economic dilution, it would have affected the shareholders that owned AIG stock at the time of the exchange on January 14th, 2011, not shareholders that owned stock on June 30, 2009.

So, just slightly different issues, that the share price changed over the 1 1/2 years between June 2009 and January 2011, but so does the composition of shareholders. So, in other words, if anybody was damaged, it would -- theoretically, if they were damaged, it would have been on January 14, 2011, not on June 30, 2009. And the composition of shares changed a lot in terms of the ownership of those shares over that 1 1/2 years.

Q. Did you investigate whether the AIG shareholders changed after June 30th, 2009?

A. Yeah. I looked at -- if you will turn to the next demonstrative, 2767, the total number of shares outstanding on both June 30, 2009, and December 31st, 2010, according to that data, it was 134.6 million. So, the number of shares outstanding were unchanged.

We ended up with the ownership of the shares by institutional investors on those two different dates, and as you can see, on June 30, 2009, institutional investors owned 38.8 million of those shares, and as of December 31st, 91 million. So, there was a tremendous increase in the institutional ownership of the shares or a change in the composition of ownership between June 30, 2009, and December 30, 2010.

So, the percent owned by the institutional investors as of June 30, 2009, was 29 percent, and it increased to 68 percent by December 31st, 2010. So, it's not just the stock price that changed but the composition of the ownership that makes the chronological issues very important in terms of comparing what actually happened in January 2011 to what happened in June of 2009.

Q. Okay. And does the table in this demonstrative include any shares owned by the Government?

A. No, it doesn't.

Q. Did you identify any other issues with respect to Dr. Kothari's Series E and F preferred stock claim?

A. Yes, in terms of priority and liquidation, because preferred stock had what's called liquidation preference, and that has, you know, important implications in terms of valuation in a time in which a company enters into bankruptcy, in terms of priority of payments.

Q. Would you turn to your next slide. Can you tell us what you're setting forth in this demonstrative?

A. This is dealing with the fact that the E and F preferred stock had priority rights over common stock. So, in other words, in bankruptcy, what normally happens is that that gets repaid before preferred, and then preferred gets repaid before common. So, generally the priority order is first debt and secondly preferred and third common.

And then Dr. Kothari claims that the fair value, which is point 2, of the E and F preferred stock was less than their liquidation preference; in other words, their value is less than the values that they were guaranteed in liquidation under the E and F preferred contracts.

Q. Before you go on, I want to go back to this priority rights issue that you have in your first bullet or first point there. Did the priority rights affect AIG's ability to pay dividends to common shareholders?

A. Yes. The Series E and F preferred stockholders had a right to prevent dividends being paid to common stockholders.

Q. And what is your understanding, if any, about AIG's ability to pay dividends to common shareholders as long as the Series E and F preferred stock was outstanding?

A. Well, as I said, they could not pay dividends and they could not repurchase stock from common shareholders. So, common stockholders would be constrained to receiving no dividends and not having their stock repurchased as long as E and F preferred stock remained out there.

Q. Okay. Now, you were talking about the liquidation preference in your second point. Would you continue with that.

A. Yes. The liquidation preference means that E and F should get their face value in liquidation. Dr. Kothari claims that the fair value that they would receive was less than their liquidation value. So, if that was true, that they couldn't pay off the preferred shareholders in full, in other words, the liquidation value, you can only pay off part of their value, which he claims to be the fair value, which was less than liquidation value, the logical implication is that since common stockholders follow preferred stockholders in terms of priority, the value of their claims would be zero, which is point 3.

So, it just says if it Dr. Kothari's correct that the fair value is less than liquidation value, then both the common stock and the stock split class claim would be zero as of January 30, 2009.

Q. I want to turn back just to tie down a fine point on something we've already discussed. We were talking about the Series C preferred stock, do you recall that, a few moments ago?

A. Yes.

Q. And I think I asked you if the trust -- there were two options that you discussed to monetize the

Series C, and I had asked you about whether the shareholders -- whether they're required -- to monetize, whether there was a separate vote required by the common shareholders. Do you remember that?

A. I recall that, yes.

Q. Now, why, if at all, is it relevant that the Series C preferred stock could be more liquid than the common shares if the trust monetized it under either of those two options that you described?

A. Because then the -- there would be no illiquidity premium having to be paid on exchange in Dr. Kothari's world of the Series C preferred for common stock. There is an alternate way to monetize that actually might lead to common stockholders paying the preferred premium not to monetize, using either methods -- the two methods I mentioned.

So, the -- in my view, the 339 million does not make sense in terms of the options that were available there to monetize, and Dr. Kothari just looks at one option, which is -- you know, which he claims is a liquidity payment to effect the exchange, but there were ways either through the ADR method or the redenomination method and registration itself that the preferred -- would not lead to this so-called claim of 339 million and a claim of an illiquidity premium being paid by the preferred shareholders to the common shareholders.

Q. Thank you.

Your Honor, may I have one moment?

THE COURT: Sure.

(Counsel conferring.)

MR. ROBERSON: Your Honor, at this time, I'd like to move in the demonstratives that we have just gone through, DX 2701 through DX 2768.

THE COURT: Okay.

MR. BOIES: No objection as demonstratives, Your Honor.

THE COURT: All right. Defendant's Exhibits 2701 through 2768 are admitted as demonstrative exhibits.

(Defendant's Exhibit Numbers 2701-2768 were admitted into evidence.)

MR. ROBERSON: And, Your Honor, at this point, we pass the witness.

THE COURT: All right. Why don't we take a lunch break and then we will start with the cross after lunch. Let's reconvene at 1:35.

(Lunch recess, 12:35 p.m. to 1:35 p.m.)

AFTERNOON SESSION

(1:36 p.m.)

THE COURT: Thank you. Please be seated.

He let's go ahead with cross, Mr. Boies.

MR. BOIES: Thank you, Your Honor.

CROSS EXAMINATION

BY MR. BOIES:

Q. Good afternoon, Professor Saunders.

A. Good afternoon, Mr. Boies.

Q. I'd like to begin with the Series C, E, and F exchanges, which was the last subject that the Defendant talked to you about, and I'd like to begin by starting at your Defendant's Exhibit 2766, and one of the points that you were making was that the exchange took place at a different time than the reverse stock split took place.

A. Correct.

Q. Correct?

A. I'm sorry, Mr. Boies. Could you make it a little bit closer? I've had eye surgery, and it would help me just to see, because I --

Q. All right.

A. That would be fine.

Q. Is that good?

A. I think I can see it now, yes.

Q. And the Series C, E, and F exchanges took place January 14th, 2011. Is that right?
A. Correct, yeah.
Q. And the reverse stock split was 6/30/09. Is that right?
A. Yes.
Q. Now, do you understand that the reverse stock split on June 30, 2009, was necessary for the Series C, E and F exchange to take place on January 14th, 2011?
A. I believe it created room for enough shares to do the exchange.
Q. And you've reviewed the trial transcript in this case, have you?
MR. ROBERSON: Objection.
THE WITNESS: Only a couple of witnesses. That's all.
BY MR. BOIES:
Q. Only a couple of witnesses?
A. Yeah.
Q. Which witnesses were those?
A. Bernanke, Geithner, of course.
Q. You didn't look at the trial testimony of Mr. Brandow?
A. No.
Q. But you do understand that if there had not been

a reverse stock split or some other increase in the number of authorized shares, the exchange that took place on January 14th, 2011, could not have taken place, correct?

A. Either the stock split or an increase in the number of authorized shares.

Q. Now, turning to your Exhibit 2768, you say that if the fair value of the Series E and F preferred stock was less than their liquidation preference, then the common stock would not have any value.

A. Yes.

Q. Let me push you a little bit on that, if I may, sir.

A. Okay.

Q. The reason or one of the reasons that the fair value of the Series E and F preferred stock is less than their liquidation preference is simply net present value, correct?

A. This is -- first of all, I have not valued them myself. So, I have just seen Dr. Kothari's claims about the fair value. I'm not quite sure which valuation you're referring to.

Q. Well, there are lots of reasons why the fair value of a preferred stock that has no right on the part of the holder to be redeemed and no right to receive dividends would be less than the liquidation value of that stock, correct?

A. I don't know. I didn't -- I didn't investigate it. I'm sorry.

Q. Well, as a financial economist, you know that there is a time value to money.

A. Correct.

Q. And you know that if I have a right to get a thousand dollars today, that's worth a thousand dollars, correct?

A. Correct.

Q. But if I have the right to get a thousand dollars at some indeterminable point in the future, that's going to be worth less than a thousand dollars, correct?

A. That's correct.

Q. Okay. Now, the liquidation preference for the Series E and F stock was the right to get that liquidation preference perhaps at some indeterminable time in the future, correct?

A. I believe the company had the right to call the stock in.

Q. The company had the right to call the stock in, but the shareholder, the Government, did not have the right to force the redemption, correct?

A. Correct.

Q. So, you have this Series E and F stock, and the holder of that stock can't get the liquidation preference unless the company agrees, correct?

A. Or the company goes illiquid.

Q. Or the company goes illiquid. And as a result, the Series E and F stock are going to have a fair market value of less than their liquidation preference, correct, sir?

A. Unless the company wants to call the shares in early.

Q. Unless the company calls the shares in, the Series E and F stock is going to have a fair market value of less than its liquidation value, correct?

A. That's correct, yes, if it doesn't call the shares in.

Q. Okay. And that's going to be true even if the company is doing very well and has lots of assets and lots of value, correct?

A. Yes, because it depends on the call option of the -- of the company.

Q. Yes. And so you can have a fair market value for the Series E and F stock that is less than their liquidation value and still have a lot of value in the common stock, correct?

A. I'm not so sure -- well, are you asking in this case or in general?
Q. Well, let's begin with --
A. Because -- because E and F shareholders had the right to prevent the company from paying dividends on the common stock and to doing repurchase of common stock. So, I'm not clear about your hypothesis that the value of the common would be positive.
Q. The value of the common being positive is not related to whether the Series E and F stock will trade at their fair market value, correct, sir?
A. Well, I'd say that if --
Q. That's a yes or no answer or I don't know.
A. I'm sorry. Could you just repeat that back, please? Sorry.
Q. Sure. The common stock can have a positive value even if the Series E and F stock will trade below their liquidation value, correct, sir?
A. Again, are you assuming away -- I just want to understand your hypothetical -- the preferred stock restricting the common stock dividends and preferred stock restricting stock repurchases?
Q. No, I'm not -- I'm not --
A. You're assuming a hypothetical where the common stock can receive dividends and can receive -- make a

repurchase of common stock?

Q. No, I'm not assuming that. I'm trying to -- I'm trying to tell you, I'm not assuming that.

A. Okay.

Q. I'm trying to take the E and F stock just the way they were -- and let me put the question this way. As a financial economist, if the Series E and F stock were trading in the marketplace --

A. Um-hum.

Q. -- on January 13th, 2011 --

A. Um-hum.

Q. -- and there was no obligation on the company to exchange them, would you expect the Series E and F stock to be trading at their liquidation value? That's a yes or no or I don't know.

A. I don't know.

Q. Would you ordinarily expect that a series of preferred stock that has the right to block dividends and block common stock repurchases, but does not have any right itself to command dividends or repurchase, would ordinarily trade below its liquidation value?

A. I didn't consider that. So, your hypothetical is that the common stock cannot receive anything, any cash flow?

Q. Yes.

A. And the preferred stock -- because you're waiting for the call option to be called?

Q. Yeah.

A. Your hypothetical is that the common stock doesn't care that they're not receiving dividends and they're not being able to repurchase shares that they don't --

Q. That's not my hypothetical.

A. -- that they don't call the stock.

Q. That's not my hypothetical.

A. Okay. I'm sorry, sir. I misunderstood.

Q. My hypothetical is simply a situation where you have a preferred stock that has a blocking right, a blocking right on common stock repurchases, a blocking right on dividends, but does not have the right to force its redemption or to receive dividends or to accumulate dividends.

A. Um-hum.

Q. And you understand that those were all the characteristics of the actual E and F stock, correct?

A. That's correct. They were noncumulative.

Q. Right. And what I'm asking you is, as a financial economist, would you ordinarily expect that preferred stock to trade below its liquidation value?

A. Well, the further out you push it, the lower its

present value, that is correct.
Q. And the lower --
A. Given those conditions that you just stated.
Q. Okay. And that would be true regardless of whether the company was solvent or not; that is, you could have a solvent, functioning, profitable company, and that still would be true simply because of the net present value of money, correct?
A. Yes, assuming that they don't want to call the stock because they're not earning any dividends or being able to repurchase shares and that the common stock would be close to zero value.
Q. I want to be sure I understood what you just said.
A. Yeah.
Q. Did you say that if you have common stock that's not earning any dividends and is not able to be repurchased, that the value would be close to zero?
A. Well, because --
Q. I'm just asking, is that what you said?
A. I'll try to explain.
Q. No, first --
A. Yes, I did. Yes.
Q. Now, you know a lot of companies that pay no dividends and are not repurchasing stock where the

common stock value is far above zero, correct, sir?
A. But there --
Q. Yes, no, or I don't know.
A. But there is no blocking stake there. They don't have preferred shares blocking their ability to convert.
Q. Sir --
Your Honor?
THE COURT: Let's try to listen to the question and answer exactly what's asked.
THE WITNESS: Yes, I'm sorry. I'm trying to formulate it in my mind.
BY MR. BOIES:
Q. There are a lot of companies that pay no dividends and don't intend to pay any dividends in the near future and are not repurchasing stock where the common stock value is far above zero, correct, sir?
A. I don't know.
Q. Ever heard of Google?
A. I don't know that they can't repurchase stock or not.
Q. I didn't say they couldn't, but they're not, are they? They're not repurchasing stock and they're not paying dividends.
A. But they have an option to repurchase if it has

value.

Q. Yes, but do you think --

A. Value to shareholders is an option different from not having the option at all.

Q. Of course it's different, sir, but you're not saying that that difference would bring the stock price down to zero, are you?

A. If they have that option to pay, yes, but I thought your hypothetical was in the case you couldn't repurchase at all or you couldn't pay dividends at all.

Q. If --

A. If they have the option, of course, it has value.

Q. But even if they don't have the option to pay dividends, the Google stock wouldn't be zero, would it, sir?

A. What if they can't pay dividends and they can't repurchase the shares and you have no option for value because it's blocked? You can't exercise that option.

Q. But it's not blocked forever, is it, sir, because they can unblock it any time they want by redeeming those preferred shares.

A. If this is a hypothetical outside the case we're thinking about, yeah. I mean, I agree with you if there's no preferred shares blocking the conversion.

Q. So, we have got actual Series E and F stock that could block dividends and common stock repurchases, right?

A. Okay.

Q. And it has no right to redemption or dividends, it is noncumulative, and it is subject to call by the company for the liquidation value. Now, that stock you would expect to trade below its liquidation value, correct?

A. Unless the probability of liquidation was very high.

Q. Okay. And, indeed, it would trade below its liquidation value even if the probability of liquidation is very high unless the probability of liquidation was certain, correct, sir?

A. Yes. As long as it's not one, it would trade below that price.

Q. And that would be true whether or not the company itself was profitable or not, correct?

A. It could have profits, that's true.

Q. Now, did you make any effort to determine what the fair value of the Series E and F preferred stock was as of either June 30, 2009, or January 14th, 2011?

A. No.

Q. In the course of your investigation, did you see estimates of the fair value of the Series E and F preferred stock?

A. In Dr. Kothari's report I saw some estimates.

Q. Other than in Dr. Kothari's report, did you see anything?

A. Not that I can recall.

Q. Did you see, for example, a Department of Treasury estimate of the fair value of the Series E and F preferred stock?

A. At what date, sir?

Q. One would have been as of 2009 and another would have been in 2010, either one.

A. That's not the exact dates that you asked me. You asked me did I see anything to value it as of those dates, you said the 14th of January and the 30th of June.

Q. Let me try to be clear. Did you see any estimate of the value -- the fair value of the Series E and F stock other than Dr. Kothari's?

A. No.

Q. Okay. Did you look for it?

A. No.

Q. Okay. Let me turn now to your testimony about the Series C stock, and one of the things that you say is that the Series C stock could have been monetized in ways that did not require it to compensate the stock split class.

A. For a liquidity premium.

Q. Well, would it have had to compensate the stock split class for some other reason?

A. Not that I am aware of, no. They could request the exchange. I don't understand the question. You're expecting some answer that I'm not quite sure what the question is.

Q. I asked you about your testimony that the Series C stock could have been monetized in ways that did not require it to compensate the stock split class. You then said "for a liquidity premium." Do you recall that?

A. Well, I said rather than paying a liquidity premium, they had two other ways to monetize the shares, and that's what I discussed in my report.

Q. Now, you're not a lawyer, correct?

A. No.

Q. And you didn't make any effort to determine whether either of these two approaches would have been legally permissible, correct?

A. Correct.

Q. The option that you refer to -- I'm sure it was entirely inadvertent, but I got two copies -- in my binder, I got two copies of one of your charts and no copy of the other.

A. Do you want my copy, then?

Q. If you look at Defendant's Exhibit 2763, one of those options is depository shares. Do you see that?

A. Yes.

Q. And you cite Joint Exhibit 185 at Section 6.7, correct?

A. Yes.

Q. And that is a stock purchase agreement dated March 1, 2009, correct?

A. Correct.

Q. Before March 1, 2009, was there any way for the trust to have entered into a depository arrangement whereby the Series C preferred stock would be deposited and the depository shares would be issued in denominations specified by the trust?

A. I don't know.

Q. Okay. Did you investigate at all how it came to be that this provision was added to the stock purchase agreement when it was executed on March 1, 2009?

A. No.

Q. Do you know whether or not that was added in response to a lawsuit referred to as the Walker lawsuit?

A. No.

Q. Have you ever heard of the Walker lawsuit?
A. Vaguely.
Q. Do you have an understanding of what the Walker lawsuit was?
A. I'd have to try to remember, but I think it was to do with a shareholder bringing claim against the Government.
Q. And do you recall that in response to the Walker lawsuit, there was a representation to the Court that AIG would not increase its authorized shares without a class vote of the common shareholders?
A. I don't know, sir.
Q. Let me go to your chart, Defendant's Exhibit 2764, where you talk about an option of registering the Series C preferred stock to sell it publicly.
A. Yes.
Q. And a necessary step there would be to redenominate the total Series C preferred stock so that you would break it up and you'd have several billion shares of it as opposed to the small number that actually existed, correct?
A. That is correct, yes.
Q. And that would have required the approval of AIG, correct?
A. In terms of a shareholder vote? I believe it

did not require a shareholder vote.
Q. It would have required either a shareholder vote or AIG board action, correct?
A. I don't know.
Q. And I take it you did not investigate whether either of those would have been legally permissible.
A. No.
Q. Did you form an opinion or a conclusion as to whether, in January, February, and March of 2009, the Government was a controlling shareholder of AIG?
A. It had a 79.9 percent stake after the Series F was issued.
Q. And recognizing that you're not a lawyer and I'm not asking you for a legal opinion, but did you investigate whether the Government believed that because of its controlling shareholder position, there were limits on what it could do?
A. No.
Q. Let me turn to the chart in which you analyze whether or not there was economic loss to the shareholders as the result of what you refer to as the rescue transaction, and let me ask you to begin with --
A. Can you just tell me which demonstrative?
Q. -- 2745. And 2745 is a chart where you compare the AIG market capitalization based on the September

16th opening price to the market capitalization based on the September 17th opening price, correct?
A. Correct.
Q. And the market capitalization of AIG based on the September 16th opening price is $5 billion, correct?
A. That's correct.
Q. And the market capitalization of AIG based on the September 17th opening price is $32.9 billion, correct?
A. Yes.
Q. And you attribute that increase in market capitalization to the credit facility that the Government had offered to AIG, correct?
A. That's correct.
Q. Now --
A. The green -- the green box, yes.
Q. The green box.
A. Yes.
Q. The green box is $26.7 billion, and then the shaded --
A. And the shaded value is --
Q. -- value is $1.2 billion.
A. Yes, that's correct.
Q. And so there's a total increase in the market capitalization of AIG of $27.9 billion, correct --

A. Yes.

Q. -- of which $1.2 billion is captured by the common shareholders, correct?

A. That's correct, the original -- the original shareholders, yes.

Q. And $26.7 billion is captured by the Government, correct?

A. The new shareholders.

Q. And the new shareholders are the Government.

A. Correct.

Q. If the Government had made the revolving credit facility available for the same interest rate and the same fees and terms, except not required the 79.9 percent of the equity, then the entire $27.9 billion of increased value would be captured by the common shareholders, correct?

A. That is correct.

Q. And you have not made any investigation or analysis as to whether the Government was or was not authorized to demand the 79.9 percent of the equity, correct?

A. I'm not quite sure what you mean, "authorized."

Q. Whether it was legal for the Government to do that. You haven't investigated that.

A. I'm not a lawyer, no.

Q. Well, not only are you not a lawyer, but you didn't investigate that issue, correct?
A. Well, it seems to be a legal issue to me, sir.
Q. Did you investigate the extent to which in other Federal Reserve loans the Federal Reserve had demanded equity?
A. What type of loans are we talking about?
Q. Are you aware of any Federal Reserve loans of any kind, at any time, other than the AIG loan, where the Federal Reserve demanded equity?
A. In recent years, no, but I don't know what happened with our history back to 1914.
Q. You know that there were loans pursuant to Section 13(3) of the Federal Reserve Act in the 1930s, correct?
A. That is correct.
Q. And as part of your investigation and analysis, did you review information about those loans?
A. No.
Q. Not at all?
A. No.
Q. As part of your investigation and analysis, did you review information about Federal Reserve 13(3) loans that were made in 2008 and 2009?
A. Yes, I did.

Q. And did you discover that there were a significant number of companies that received 13(3) loans in 2008 and 2009?
A. I think it was five companies, including AIG.
Q. Five companies?
A. Well, I think it was Bear Stearns, AIG, and Fannie Mae and Citibank and Bank of America.
Q. And you think those are the only five companies that received 13(3) loans from the Federal Reserve in 2008 and 2009?
A. Individual -- I mean, are we talking about individual or are you talking about, you know, broad facilities of 13(3)? So, I understand you were asking about individual facilities.
Q. My question is, what companies received 13(3) loans in 2008 and 2009 from the Federal Reserve?
A. You mean in general, then, through broad facilities? I'm just trying to redefine the question, that's all.
Q. I know you're redefining the question, but I'm asking you to focus on my question.
A. So, I'm trying to answer your question as best I can.
Q. Okay, okay. My question is approximately how many companies, to your understanding, received 13(3)

loans from the Federal Reserve in 2008 and 2009?
A. Through both individual facilities and broad facilities?
Q. I don't know what you mean by "individual facilities" and "broad facilities" --
A. Well, individual --
Q. -- and I'm trying to avoid getting into definitional issues. I'm simply asking a very simple question, all right? How many companies received 13(3) loans from the Federal Reserve in 2008 and 2009, if you know?
A. I mean, I've never counted up --
Q. Do you have any approximation?
A. It's five plus those that had access to the PDCF and the other broad lending facilities under 13(3).
Q. Any idea how many that works out to?
A. I never counter.
Q. A hundred?
A. I don't know.
Q. Do you know whether any of those companies that borrowed money had to surrender equity?
A. I don't believe any did. To the Federal Reserve we're talking about now, not to the Treasury?
Q. You understand that --
A. I'm just trying to understand the question. Is

it the Federal Reserve we're talking about?

Q. You understand that the Federal Reserve loaned money pursuant to Section 13(3).

A. That's correct.

Q. You understand the Treasury did not do that, correct?

A. That's correct. So, I just wanted to make sure that I'm answering your question as best I can.

Q. And you understand that the Treasury made, through the TARP program, investments in preferred stock.

A. That's correct.

Q. And you understand that the Federal Reserve, other than AIG, never did that, correct?

A. That's correct.

Q. Now, on Defendant's Exhibit 2745, you compare the market capitalization of AIG based on the September 17th opening price with the market capitalization based on the September 16th opening price.

A. Correct.

Q. The price on September 16th at the close was higher than the price either on the 16th opening or the 17th opening, correct?

A. That's correct.

Q. Did you form an opinion or a conclusion as to why the AIG stock price declined from the September 16th close to the September 17th opening?

A. Because my -- I viewed the 16th --

Q. Sir, my question is whether you did it or not.

A. No.

Q. Okay. In addition, are you aware that the stock price on September 24th declined from the AIG stock price on September 23rd?

A. On the close, yes, not on the opening.

Q. Was the opening on September 24th higher than the opening on September 23rd?

A. I don't know. I'd have to look at my price graph, but I'm pretty sure it wasn't higher compared to the close on the 23rd. I thought that was the question.

Q. Did you think we were comparing -- and I'm just asking --

A. No, I'm just asking if I could look at my demonstratives to refresh my memory --

Q. Absolutely. Just tell me which one you're looking at.

A. -- so I can answer your question as precisely as I can.

Q. Just tell me which one you're looking at.

A. I'm trying to find it.

Q. Would it be 2751?

A. Yeah, I'm trying to -- yeah. 2751 you think? There is a chart with all the openings and closings. Yes, that's good. Okay, fine.

Q. Now, the closing price on September 23rd is $5, correct?

A. That's correct.

Q. And the closing price on September 24th is $3.31, correct?

A. Correct.

Q. And the opening price on September 23rd is $5.38.

A. That's correct.

Q. Correct?

And the opening price --

A. $5.34 -- $5.38 on the 23rd opening, yes.

Q. And it's $5.34 at the opening on the 24th, correct?

A. Yes, that's correct.

Q. Now, did you study why there was a decline from the closing price on September 23rd to the closing price on September 24th?

A. No, because I think -- I assume the opening price --

Q. All I asked you is whether you did it or not, sir.

A. No. I didn't think I needed to.

Q. Okay. Did you investigate at all why the stock price declined on September 24th from $5.34 to $3.31?

A. Yes, I did look at news information that was coming out over the course of the day, and a lot it was very negative for AIG.

Q. And did you conclude why the stock dropped from $5.34 to $3.31? Did you do, for example, an event study?

A. No, I did not.

Q. Let me ask you about something that you said with the Government. You said that you used the September 17th opening price, as shown on Defendant's Exhibit 2745, because you concluded that it was an efficient market and the market had absorbed all of the relevant information that was available. Do you recall that?

A. Yes.

Q. What I want to focus on now is what information was available at the September 17th opening.

A. Um-hum.

Q. Do you believe that the substance of the revolving credit transaction was available to the marketplace?

A. Yes.

Q. Do you believe that there were any significant elements of the revolving credit transaction that were not available to the marketplace the morning of September 17th but became available to the marketplace thereafter?

A. No.

Q. On the morning of September 17th, do you have an opinion or a conclusion as to what the marketplace believed the form of equity would be?

A. No.

Q. Did you investigate that at all?

A. It isn't possible, because it's -- the stock price is showing the confluence of different opinions as to what it might be. So, basically, it reflected investors' beliefs as to what it might be. Some might have different opinions, some might think it's preferred, some might think it's common, some might think it's warrants. So, it is just a general consensus opinion, efficient statistic as of the morning of the 17th.

Q. You think that on the morning of the 17th, some market participants believed that the equity component would be preferred stock. Is that what you just said?

A. It could have been anything. They just said 79 --

Q. No, no, not my question.
A. -- convertible preferred -- convertible preferred, I should say. Sorry.
Q. Is it your understanding and belief that on the morning of September 17th, some market participants believed that the equity component would be what you refer to as convertible preferred stock?
A. It was a 79.9 percent stake, so it could have been in many different forms.
Q. That's not my question, sir.
A. It's -- convertible preferred stock is possible; warrants was possible.
Q. All of that is possible.
A. Common stock was possible.
Q. All of that is possible, correct? Correct?
A. That is correct.
Q. Now, did you investigate at all what you thought, as a financial economist, the market believed on the morning of September 17th the form of equity would be?
A. As I say --
Q. No, just -- just answer the question. Did you investigate --
A. -- I realized that the stock price was an efficient statistic which revealed what the market

thought as to the form of the equity, and it could have taken many different forms.

Q. Did you investigate at all what you thought, as a financial economist, the market believed the morning of September 17th the form of equity would be?

A. I don't know how I would do that. All I know is that they knew it was 79 --

Q. You don't know how to do that?

A. Well, I don't know how to decompose a whole market's opinion as to what form of equity there would be at the opening on the 17th. Over the day, there were analyst reports that differed according to what type of equity form would be the result of the rescue transaction, but I'm talking here about the opening price.

Q. Let me see if I understand what you're saying. You're saying that -- you're talking about the opening price here, and during the day, information came out about what the form of equity might be, but that information was not available in the morning?

A. No, it was available in the morning as well, because there was a difference of opinion.

Q. Did you come across any news articles, analyst reports that expressed a difference of opinion as to what the form of equity would be?

A. Well, some just said 79.9 percent in a form to be determined, and there were some that said in the form of warrants.

Q. What did you see in terms of news reports or analyst reports the morning of September 17th that said it would be 79.9 percent equity in a form to be determined?

A. I think I might have quoted a few of them in my report. I vaguely remember, but I did see some that said 79.9 percent.

Q. Do you have your report up there?

A. Yes.

Q. Why don't you identify for me the news reports or analyst reports that the morning of September 17th said that the equity would be in a form to be determined, and just tell me what page you're referring to.

A. Well, if you can give me a few minutes, let me just try and find them.

Q. When you have it, let me know.

A. It's a long report. (Document review.) Anyway, I don't know if it's here, but I do remember looking at analyst reports, and there was a dispersion between it. But where it is, I'm not sure.

Q. When you find the news reports or analyst reports that on the morning of September 17th said that the equity would be in a form to be determined, please let me know.

A. (Further document review.) I believe it was somewhere in here or at least -- if it's not here, I did consider them. I think it's here, but I'm not quite sure where.

Q. Go ahead. Take your time.

A. Well, I did look. I can't find it.

Q. Take as much time as you need.

A. I know there were a number of reports. Some were very general about the form and some said warrants. There was no consensus as far as I remember. And I thought I put that in my report, but if it's not here, it's not here.

Q. You did put in your report everything you relied on, didn't you?

A. I thought I did. If it's not there, then it's an oversight, but I was pretty sure that I did put it in my report, but if it is not here -- although I do recall reading in this report that there was a dispersion of opinion.

Q. When you say that you do recall reading in this report that there was a dispersion of opinion, do you mean that you're reading somewhere in there that on

September 17th, the morning, there was analyst reports or news articles that said the form of equity was to be determined?

A. Some said 79.9 percent equity stake and some said warrants.

Q. Did any of them say "form to be determined"?

A. Perhaps not the form to be determined, but a 79.9 percent equity stake.

Q. Sir, you would -- you're not saying that you saw any analyst reports or news articles on the 17th that said "form to be determined." Fair?

A. I'd have to go back and look at them, but I know they said 79.9 percent equity stake, and it didn't specify the form.

Q. Now, take a moment and now see if you can find in your report any reference to articles or analyst reports as of the morning of September 17th that simply said "79.9 percent equity stake" and did not mention warrants.

A. Well, I thought it was here.

MR. ROBERSON: Would it be helpful if I pointed to a page of the report, Your Honor?

THE COURT: I don't know.

THE WITNESS: It's a long report.

MR. BOIES: I suppose it depends who's the real author of this report.

THE WITNESS: No, I wrote this, just I thought it was here. Actually, I have got it now by luck, page 19 and page 20.

BY MR. BOIES:

Q. Page 19, and this is Defendant's Exhibit 1882?

A. This is different sources on the --

Q. What I'm trying to do is there are two different exhibits that counsel have given us, 1882 --

A. Paragraph 42 of the report, page 19, carrying onto page 20.

Q. And the Morgan Stanley document that you cite there --

A. Yes.

Q. You cite three documents here, right?

A. Yes.

Q. A Morgan Stanley, a Wachovia, and a Credit Suisse?

A. Yes.

Q. And are those documents included in your appendix somewhere?

A. In terms of documents cited?

Q. Yes.

A. I'm not sure.

Q. Let me try to pull those out.

THE COURT: Mr. Roberson?

MR. ROBERSON: Well, it says "Kothari Source Document" for all three of those.

BY MR. BOIES:

Q. And we will -- we will try to pull those out so that we can show them to you --

A. Um-hum.

Q. -- unless counsel for the Government wants to hand them up. I'm happy to take their help on this one if they have them.

MR. ROBERSON: I don't have them with me, Counsel.

MR. BOIES: Okay. Then we'll try to find them.

BY MR. BOIES:

Q. In the meantime, let me turn to another subject, and we'll come back to this one when we can find those three documents that you -- that you're referencing.

In that connection, let me go to the area of risk, and you said that, ex ante, you believed that there was a lot of risk in this loan, correct?

A. Ex ante, at the time the loan was made on the 16th, the risk was high, yes. The credit risk was high.

Q. Now, you would agree, would you not, that when you're looking at the risk of a loan, you want to look at the risk with the loan made, not before the loan is

made, correct?
A. No. The thing is you don't want the money to exit the door until you're pretty sure you're going to be repaid.
Q. Of course, sir, but my point is, you're going to be repaid after the loan is made, correct?
A. You hope so.
Q. Yes, indeed. And what your analysis is in terms of repayment is whether the borrower will be able to repay it if you give the borrower the loan, correct?
A. Yes. It's ex ante, correct.
Q. Whether it's ex ante or not --
A. But it's before the loan is made.
Q. -- you're making the analysis be --
A. Before the loan is made.
Q. -- before the loan is made, correct?
A. Correct.
Q. But you're making the analysis before the loan is made about what is going to happen if you make the loan, correct?
A. You form an expectation about what might happen.
Q. The effort --
A. The probability of the loan being repaid based on your expectation as of the date the loan is made, which is the probability of default. So, you assess two

variables, the ex ante probability of default and the loss given default, the severity.
Q. My question is a simple one. When you're making a determination before you make a loan about whether that loan will be repaid, you take into account the effect on the borrower of receiving the loan, correct?
A. Again --
Q. Yes, no, or I don't know.
A. No. I would say no.
Q. Okay.
A. You have an ex ante expectation about the probability of the borrower defaulting.
Q. So, your answer to my --
A. You don't know what he's going to do with the money. He could steal the money. So, you don't know if he's going to use it in any productive fashion. So, you have an ex ante view. It's all ex ante.
Q. I just want to be sure that I've got the record clear before I go to your textbook, okay?
A. Yeah.
Q. When you're making a determination of whether to make a loan, recognizing that that's going to be made before you make the loan, and you're trying to determine whether that loan will be repaid, you take into account the effect on the borrower of receiving the loan. Yes

or no.

A. You take into account the riskiness of what the borrower might do with the money, yes, ex ante. In other words, he might not invest it, he might steal it, he might invest in a project that he applied for. It's called reshifting. So, once the money is out of the door, the borrower has many options on what to do with the money. So, you assess an ex ante probability expectation as to his repayment probability.

MR. BOIES: Your Honor, could you ask the witness to try to answer my questions yes or no? And I know he has many things to say about them, and he may get a chance on redirect, but I would like to just get answers to my questions.

THE COURT: Sir, I know you have the ability to listen to the question and give a precise answer.

THE WITNESS: Yeah.

THE COURT: So, once again, that's what you need to try to do.

THE WITNESS: I will try to do that.

BY MR. BOIES:

Q. With respect to AIG, the Government knew what AIG was going to do with the money, correct?

A. It needed the liquidity, that's correct.

Q. And the Government had a number of covenants designed to ensure that AIG did with the money what the Government wanted AIG to do with the money, correct?

A. Well, most loan contracts have covenants, that's correct.

Q. Well, this loan had more covenants than the usual loan, correct?

A. That's a very big question. I mean, when you make a loan to a distressed company, you generally have more covenants than to a nondistressed company.

Q. Did you make an assessment as to whether the covenants with respect to the revolving credit facility were significantly greater than the covenants in private loan transactions with which you were familiar? That, again, is a yes or no answer, sir.

A. Can I just qualify it slightly?

Q. Could you start with a yes or no?

A. So, if you could just repeat the question.

Q. Sure.

Did you make an assessment as to whether the covenants that existed in the revolving credit facility were significantly greater than the covenants in private loan transactions with which you were familiar?

A. Okay. I did make an assessment, because it was very similar to private loans to distressed companies, which is very different from loans to a nondistressed company.

Q. Were you aware or did you come across in your investigation any statements by either the Government or AIG that took a position contrary to what you just said?

A. I'm sorry. Can you just repeat the question?

Q. Were you aware or did you come across in your investigation of any statements by either the Government or AIG that took a position contrary to what you just said?

MR. ROBERSON: Objection. Compound and vague.

THE WITNESS: I'm trying to understand. I'm sorry, I'm trying to understand your question.

THE COURT: Let's see if we can break it up a little bit.

MR. BOIES: Sure, Your Honor.

BY MR. BOIES:

Q. You said that you made an assessment that the covenants in the revolving credit facility were very similar to private loans to distressed companies. Do you recall saying that?

A. Yes, I just said that. Yes.

Q. And my question is, are you aware of anything -- and I'll break it up between the Government and AIG -- are you aware of anything that the Government said or government officials said that were contrary to your view?

A. No.

Q. Are you aware of anything that AIG or representatives of AIG said that were contrary to your view?

A. No.

Q. When you say that the analysis was ex ante, you're talking about an analysis that was made on September 16th. Is that correct?

A. That's correct.

Q. In your work, did you come to understand that the Government continued to make an analysis of the extent to which the loan was or was not a risky loan?

A. Yes. There's an assessment about a collateral value that followed the making of the loan.

Q. And under the credit agreement, the Government didn't have to advance funds unless it was satisfied with the collateral, correct?

A. Secured to the satisfaction of the Federal Reserve.

Q. In its sole discretion, correct?

A. With the approval of the Board of the Federal Reserve, yes.

Q. Let me distinguish between two different things. The credit facility itself had to be approved by the

Board of Governors, correct?

A. That's correct, the revolving credit facility on the 16th.

Q. Then, whenever money was drawn down, the Federal Reserve Bank of New York itself had to make another judgment that the collateral that was being furnished was sufficient, correct?

A. You mean on each draw on each day?

Q. Yes.

A. I don't know.

Q. You don't know that?

A. I don't know if they did it on a daily basis, no.

Q. Well, they might not have drawn on a daily basis, but did you know that they did it every time there was a draw-down?

A. I mean, there might have been draw-downs every day. I have not seen any time series of the day-to-day draw-downs on the -- on the position.

Q. My question doesn't have to do with whether you've seen any time series. My question is simply, you understand that every time AIG drew down money, the Federal Reserve Bank of New York had in its sole discretion the decision as to whether the collateral was or was not sufficient at that time.

A. I can't remember.
Q. Did you see any statements by representatives of the Federal Reserve Bank or representatives of the Department of Treasury in September of 2008 that indicated that they did not think that the loan was risky?
A. It was a debate within the Federal Reserve I remember reading, the emails going back and forth. Some thought it was too risky, some thought it was reasonable to make the loan. So, I think there was a difference of opinion.
Q. Who were the people who thought it was too risky to make the loan?
A. Well, in --
Q. That's a question that asks for names.
A. I'm trying to answer.
Q. But my question -- I just want to be clear about my question.
A. Yeah.
Q. When I say "who," I'm looking for a name.
A. Yes, okay. Based on issues not just related to the loan, but also as to moral hazard, I think Mr. Madigan was concerned about making a loan --
MR. BOIES: Your Honor, I didn't mention moral hazard. He didn't mention it in his direct testimony.

He mentioned risk. I'm asking about risk. And, again, I would just ask the Court to ask him to please --

THE COURT: Yeah, give us the names, and then we'll go to the next question.

THE WITNESS: So, I am just trying to distinguish net of -- because the opinion that I'm familiar with was made related to both the ex ante credit risk and moral hazard. So, to pass out -- I don't know what Mr. Madigan's view was of the pure ex ante credit risk.

BY MR. BOIES:

Q. Well, that's what I'm asking about, sir.

A. Okay, so that's what I'm trying to answer.

Q. Okay, because you talked about the ex ante credit risk, remember?

A. Yes.

Q. And you had a number of charts about the ex ante credit risk, remember?

A. Yes.

Q. And you told me that there was a debate as to whether the loan was too risky within the Federal Reserve.

A. Yes.

Q. And what I'm asking is, can you give me the name of anybody who thought the loan was too risky to make?

A. I did see some charts that showed the collateral value --

Q. Do you -- can you give me the name of any person who thought the loan was too risky to make?

A. I can't remember. I did -- I did see charts, but I can't remember the name, just to be precise.

Q. Can you give me any name?

A. I can't remember the name.

Q. Can you give me one name, just one name of anybody in the Government who thought the loan was too risky to make?

MR. ROBERSON: Asked and answered, Your Honor.

THE WITNESS: I can't remember the name.

THE COURT: Overruled.

THE WITNESS: I can't remember the name.

BY MR. BOIES:

Q. Now, in the course of your work, you consulted with attorneys for the Defendant -- and nothing wrong with that -- but you did do that, correct?

A. Correct.

Q. And when you were trying to find out information, you would ask them questions and ask them to furnish you with information, correct?

A. That's correct.

Q. Did you ask them to furnish you with any information concerning whether there were people in the Government that believed that the loan was not risky?

A. Not risky? Well, obviously Mr. Geithner, at the time he made the loan, thought it was secured to the satisfaction of the Federal Reserve.

Q. Did you come across any information that indicated that at the time the loan was made, representatives of the Government thought that the Government was going to make tens of billions of dollars of profit?

A. No.

Q. Let me -- let me hand you a document that has been marked as Plaintiffs' Trial Exhibit 3228, which I would offer.

MR. ROBERSON: Your Honor, may understanding is this document has not been put on an exhibit list.

MR. BOIES: It is true that it is a newly marked document, Your Honor, but that's because the portion that is relevant, which is the last substantive paragraph on the first page, was a -- something that was redacted and not made available to us until very recently.

THE COURT: All right.

MR. ROBERSON: I can't speak to that myself. I'm not sure if anyone else can. They're essentially saying there' another version of this that is unredacted or that is redacted?

THE COURT: I think this is one of the documents that may have been produced following the privilege waivers.

MR. BOIES: This is a document, Your Honor, just to be absolutely clear, that we were given in the course of discovery, but what was blocked out were the last two lines on the first page and then the very first line in terms of substance on the first page.

THE COURT: Yes.

MR. ROBERSON: Your Honor, I don't think there's any foundation with this witness either, though.

THE COURT: Well, I can see the part that's coming, so it's overruled. Plaintiffs' Trial Exhibit 3228 is admitted.

(Plaintiffs' Exhibit Number 3228 was admitted into evidence.)

BY MR. BOIES:

Q. Now, this is an exchange of emails between Mr. Baxter and Mr. Huebner.

A. Correct.

Q. And you know who they are, correct?

A. Well, I know who Mr. Baxter is. I'm not sure I know who Mr. Huebner is.

Q. Mr. Baxter was the general counsel of the Federal Reserve Bank of New York, right?

A. Mr. Baxter was. I don't know who Mr. Marshall Huebner is.

Q. Would it refresh your recollection if I told you that he was a partner at Davis Polk who was the relational partner for the representation of the Federal Reserve Bank?

A. I don't know that.

Q. You didn't find that out in the work you did?

A. I didn't.

Q. In the work that you did, did you come across Davis Polk at all?

A. I have a vague recollection of Davis Polk being in play in some way in the deal, but as to their role, I don't know.

Q. Do you know who they represented?

A. Well, I think -- I believe they represented either the Federal Reserve or the Treasury.

Q. Directing your attention to Mr. Huebner's email to Mr. Baxter on September 23, 2008, at 7:22 a.m., do you see the last paragraph?

A. Yes.

Q. It says, "The real joy comes when we get back the $85" -- referring to the $85 billion in the credit facility, correct, sir?

A. That is correct, yes.

Q. -- "together with $10+++ in interest and fees, and make the treasury tens of billions it deserves (and needs!) on the equity." Do you see that?

A. That's what it says, yeah.

Q. And when Mr. Baxter responds, he says, "Thanks. Interested in the disclosure issue. Let me know when we should discuss." Do you see that?

A. Yes.

Q. He doesn't disagree with what Mr. Huebner says about the likelihood of getting paid back with $10+++ billion in fees and interest and making the treasury tens of billions of dollars on the equity, does he?

A. Well, I mean, I can't interpret the one-line response. He says, "Let me know when we should discuss." There's nothing saying yes or no, I agree with you. It just seems a very general statement. He wants to discuss it with him.

Q. Um-hum. And the statement by Mr. Huebner is pretty clear, correct, sir?

A. Well, he was looking forward with hope, as I read it, "The real joy comes..." He doesn't say it's definite; he's just hoping it will come.

Q. You don't see the word "hope" in here, do you,

sir?
A. Well, "The real joy comes..."
Q. Yes, "The real joy comes when we get back the $85 with $10+++ billion in fees and interest and make the treasury tens of billions of dollars on the equity." There's not a word in there about hope, is there?
A. No. I'm not Mr. Huebner. I don't know what he's writing. It's his view, and it's based on apparently some discussion with somebody else. That's all I can say. I'm not Mr. Huebner.
Q. All right.
A. So, what he was thinking when he wrote this last paragraph, I do not know.
Q. Okay. In connection with the work that you did, did you investigate what the Treasury and Federal Reserve had told Congress about whether the loan to AIG was or was not risky?
A. When and what committee in Congress?
Q. Excuse me, sir?
A. When and what committee in Congress? When did they tell them and to whom did they tell? That's the question. I'm just trying to understand.
Q. That's the question. What's the answer?
A. I guess that's an open question. I don't know.
Q. Well --

A. Do you mean ex post? ex ante?

Q. -- did you investigate at all what the Federal Reserve and Treasury told Congress about whether or not the loan to AIG was or was not risky? Did you investigate that?

A. I -- I'd like to hear some time period you're talking about. Are you talking about ex post or ex ante? It must be ex post you're talking about, not ex ante.

Q. Did you investigate what they told Congress?

A. That's such a general question, I can't answer.

Q. Did you investigate at all, in any way, what the Treasury and the Federal Reserve Bank told Congress at any time about whether the AIG loan was or was not risky?

A. As of what time, sir?

Q. What?

A. As of what time?

Q. I said at any time, what they told the Congress at any time. And once -- if you tell me no, then there's nothing to explore. If you tell me yes, then I can begin to focus in, but I'm just beginning to try to find out as to whether you investigated at all --

A. My opinion --

Q. -- what they said at any time --

A. -- my opinion is based on ex ante, before the loan is made.

Q. Does that mean that you did not investigate at all what the Federal Reserve and Treasury said to Congress about whether or not the AIG loan was risky?

A. Ex post, no.

Q. By "ex post," you mean after September 16?

A. After the loan was made, correct.

Q. Well, do you consider the loan having been made on September 16th?

A. I consider the funds being provided as of the 16th or promised as of the 16th.

Q. No, I used the word --

A. Committed.

Q. -- what you said was ex ante means before the loan is made.

A. Correct.

Q. Okay. Now, what I'm asking you is when, according to your testimony, was the loan made?

A. On the 16th.

Q. Okay.

A. Committed on the 16th, and the funds were drawn down over time.

Q. And when you use the term "when the loan is made," you're talking about the 16th. Is that correct?

A. The commitment to make the loan by the Federal Reserve.

Q. And that's what you meant by "when the loan was made." Is that correct?

A. Yes. The commitment to make the loan.

Q. Okay.

A. The funds were drawn down over time.

Q. Some funds were drawn down on the 16th, correct?

A. Yeah, 14 billion. Yes.

Q. And I just want to be sure I understand what you're saying. You're saying that in your view, the loan was made on September 16th, and you did not investigate anything that the Federal Reserve or the Department of Treasury said after the 16th about whether the loan was risky or not. Is that correct?

A. To Congress I thought you asked me.

Q. I did. That's what I did ask.

A. I'm not aware -- I did not investigate it. I was looking at the risk ex ante.

Q. And just --

A. Ex post could be very different from ex ante, so I'm just -- my whole issue here is ex ante.

Q. Let me ask a question, just ask a question. Did you, at any point in the work that you did, investigate what the Federal Reserve and the Department of Treasury said to the United States Congress about whether the loan was or was not risky?

A. You mean ex post, after the fact? After the 16th?

Q. Either before or after the 16th.

A. I am not aware of any before, so my -- my opinion is ex ante as of that time, and it wasn't relevant for my opinion to look ex post.

Q. Let me see if I can close this down. You are not aware of anyone from the Federal Reserve or Treasury saying anything to Congress about whether the loan to AIG was or was not risky on or before September 16th, 2008, correct?

A. On or before --

Q. That's a yes or no answer.

A. Yes, on or before, ex ante, yes. Ex ante is on or before, around the time, before.

Q. Does that mean the answer to my question is yes?

A. What was the question again?

Q. My question was, you were not aware of anyone from the Federal Reserve or Treasury saying anything to Congress about whether the loan to AIG was or was not risky on or before September 16th, 2008, correct?

A. I don't recall.

Q. Do I understand what you have said correctly that you did not investigate anything at all about what the Federal Reserve or Treasury said to Congress about whether the loan to AIG was or was not risky after September 16th, 2008?

A. As I say, I don't recall.

Q. I'm not asking you what they said to Congress. I'm just asking you whether you investigated anything at all about what the Federal Reserve or Treasury said to Congress after September 16th, 2008, about whether the loan to AIG was or was not risky. Do you understand that?

A. Yes.

Q. What's the answer?

A. I don't recall.

Q. You don't recall whether you investigated it?

A. No. I don't recall that they reported anything to Congress about the risk of the loan ex ante, as of the time they made it. I think they updated their opinion as time progressed as to the riskiness of the loan, which is ex post.

Q. Sir, I'm not asking you about ex ante or ex post. I'm simply asking you simple questions about what somebody did or didn't do, and I'd ask you to please listen to the question.

Did you investigate at all what the Federal

Reserve or Treasury said to Congress after September 16th about whether the loan to AIG was or was not risky? That is yes or no or I don't know.

A. No.

Q. Okay. Okay. Are you aware of any consultants that the Federal Reserve retained to value the collateral that AIG was pledging?

A. Are you asking after the loan was made or before the loan was made?

Q. Either one. Then, if you say you are aware, I will ask you who and when, but my first question is just are you aware of any consultants that the Federal Reserve retained to value the collateral that AIG was pledging?

A. I think, if I remember, there was a -- it was piggybacking a bit on the JPMorgan private sector syndicate loan that didn't go through with JPMorgan, came out with a collateral value on the 16th.

Q. Is it your understanding that the Federal Reserve retained JPMorgan to value the collateral that AIG was pledging for the $85 billion loan?

A. No, I'm sorry, I said piggybacking on. Basically that was a collateral value that was out there on the 16th.

MR. BOIES: Your Honor, I'm simply trying to find out whether they retained anybody to do this. I think that's a simple question.

THE WITNESS: I'm sorry. I just think they were aware of the Project North Star valuation, but they didn't retain JPMorgan directly to do that.

BY MR. BOIES:

Q. So, my question to you, sir, as you understand it, did the Federal Reserve retain anybody to help them value the collateral that AIG was posting for the revolving credit facility?

A. As of the 16th?

Q. At any time, sir.

A. I think around this time they asked Ernst & Young to come up with some valuations, but as of the time ex ante, which was -- my opinion is based on ex ante, the only one I'm aware of on the 16th was the -- JPMorgan's valuation.

Q. When, as you understand it, did the Federal Reserve retain Ernst & Young to help value the collateral that AIG was posting for the revolving credit facility?

A. I think it was after -- after the loan was made.

Q. And by when the loan was made, you mean September 16th, correct?

A. Correct.

Q. Are you familiar with a firm called Morgan Stanley?

A. Yes.

Q. As you understand it, did the Federal Reserve retain Morgan Stanley to value the collateral that AIG was posting for the revolving credit facility?

A. Yes. I think they initially asked Morgan Stanley to do it, then they switched to Ernst & Young, if I remember correctly.

Q. When you say they switched to Ernst & Young, do you mean they stopped using Morgan Stanley?

A. I believe so.

Q. When do you think the Federal Reserve stopped using Morgan Stanley to value the collateral that AIG was posting for the revolving credit facility?

A. I can't remember the exact date, but it was some date shortly after the loan was made.

Q. Sometime in September 2008?

A. I seem to recall, yes, but I'm not 100 percent sure.

Q. Did the Federal Reserve retain Morgan Stanley to help value the collateral that AIG was posting for the revolving credit facility prior to making the loan on September 16th?

A. Well, again, I remember seeing a

JPMorgan/Goldman Sachs valuation --

Q. I'm not asking you about JPMorgan and Goldman Sachs. I'm asking you about Morgan Stanley, and you understand that that's a different company, correct?

A. I do, indeed.

Q. Okay. Did the Federal Reserve retain Morgan Stanley to help value the collateral that AIG was posting prior to making the loan on September 16th?

A. I can't remember the exact date that they hired them to do that.

Q. Do you remember whether it was before or after the Federal Reserve made the loan on September 16th?

A. I can't remember.

Q. Did the Federal Reserve retain Ernst & Young to help value AIG's collateral prior to making the loan on September 16th?

A. I don't think so.

Q. Did the Federal Reserve retain Ernst & Young to help value AIG's collateral prior to signing the credit agreement?

A. I can't remember.

Q. You know when the credit agreement was signed, correct?

A. The credit agreement was signed on the 22nd, yes.

Q. Let me just ask whether you mean that's when it was signed.
A. Well, that's when I thought it was signed, yes.
Q. Would it refresh your recollection if I suggested to you that it was signed the morning of the 23rd, effective the 22nd?
A. I wouldn't know. I thought it was the 22nd.
Q. Do you know who signed the credit agreement?
A. I'd have to go back and look, but -- I can't remember.
Q. Did you review the credit agreement?
A. What, the whole credit agreement? I read part of it, yes.
Q. Who selected the parts that you read?
A. No, I had the credit agreement available. I read through it, but it's a long document. I didn't look at the appendices, et cetera, as far as I remember.
Q. You read the whole credit agreement yourself?
A. The front end of it.
Q. The front end of it?
A. Yes.
Q. How far into it did you --
A. I can't remember.
Q. What caused you to read the portions that you read?

A. It was just confirmation basically of the terms of the loan that had been agreed on the 16th.

Q. When you were reading the credit agreement, did you come to a part that addressed whether the Federal Reserve Bank could, in its sole discretion, decide whether to permit continued borrowings under the credit facility?

A. I can't remember. That seems to be a legal question.

Q. Excuse me?

A. That seems to be a legal question.

Q. Did you understand that one of the protections that the Federal Reserve had and wanted was the ability to evaluate the collateral each time there was a draw-down?

A. I don't remember.

Q. Do you understand that AIG posted certain collateral on the 16th and additional collateral in the days that followed?

A. Well, I think they did a collateral evaluation as of the 16th, but I can't remember what happened afterwards, whether the were demand notes had collateral attached to them or not.

Q. Are you saying that you don't remember whether the demand notes had collateral securing them?

A. They had collateral, but I can't remember what it was.

Q. Without remembering what the collateral was, do you remember that the collateral changed and increased as the amount of the loans changed and increased?

A. Yes, I believe so. Yes.

Q. And was the collateral that was posted for the first $14 billion in your view good collateral for that $14 billion?

A. Well, I think it was the shares of the insurance subsidiaries that was posted.

Q. Anything else, sir?

A. I can't remember.

Q. In addition to the insurance subsidiaries, did, as you understand it, AIG, the parent, have assets that were appropriate for repo financing?

A. Yes. I think they had some cash collateral, yes.

Q. And were you aware of Citibank looking at that collateral over the course of the weekend that preceded September 16th?

A. Yes. I believe so, yes.

Q. And are you aware of what Citibank concluded was the amount of money that AIG should be able to borrow on a repo basis based on that collateral?

A. I think it was around 10 billion, if I remember. Around 10 billion, if I remember.
Q. Let me ask you whether the 10 billion figure that you're referring to was the figure that Citi itself was going to lend.
A. Correct.
Q. And do you recall Citi telling AIG that there was another $20 billion of collateral that they thought could be financed in the repo market but that Citi had a firm limit of simply $10 billion?
A. I cannot remember that.
Q. In the course of your investigation, did you review the trial testimony of Mr. Schreiber?
A. No.
Q. Do you know who Mr. Schreiber is?
A. He is an executive at AIG.
Q. Do you know what his responsibilities were?
A. I think he was doing the strategic plan.
Q. And do you know that he was responsible for dealing with Citibank, to some extent, with respect to the repo?
A. No.
Q. And I take it you did not review his trial testimony?
A. No.

Q. Did you review his deposition testimony?
A. I might have. I don't remember.
THE COURT: Should we take a break, Mr. Boies?
MR. BOIES: Yes, Your Honor.
THE COURT: We will reconvene at 3:30.
(Court in recess.)
THE COURT: Thank you. Please be seated.
Please go ahead.
MR. BOIES: Thank you, Your Honor.
BY MR. BOIES:
Q. Before the break we were talking about the extent to which, if any, there was credit risk with respect to the revolving credit facility. Do you recall that, generally?
A. Yes.
Q. Now, you did not do a study of the credit quality of the assets that were pledged by AIG, correct?
A. Correct.
Q. And you did not do a net present value analysis of the credit facility, correct?
A. What do you mean by a net present value analysis?
Q. Is a net present value analysis --
A. No, of the credit facility? You mean the present value?

Q. You did not do that, correct?
A. No, that's correct.
Q. Okay.
A. I just wanted to make sure I understood what you were asking. That's all.
Q. And you're familiar with a Black-Scholes-Merton model, correct?
A. Yes.
Q. And you did not use that to value the credit facility, correct?
A. No.
Q. And you're familiar with a -- with reduced form models that are used to look at debt and other securities?
A. Yes.
Q. And you did not do that either?
A. No.
Q. In terms of the riskiness of the AIG credit facility, one of the things that you talked about was how long it would take to do asset sales. Do you recall that?
A. Yes.
Q. And one of the things you said was that there needed to be some time for asset values to recover. Do you recall that?

A. Yes.
Q. With respect to AIA and ALICO, were you aware of offers to purchase AIA and ALICO in September of 2008?
A. Oh, roughly when?
Q. In September of 2008.
A. In September 2008, I don't remember.
Q. You are aware that AIA and ALICO were ultimately sold.
A. Yes. They were sold eventually, yes.
Q. And AIG recovered approximately how much from those two entities?
A. I can't remember.
Q. Is $50 billion in the ballpark?
A. I can't remember.
Q. Do you recall that there were offers to purchase ALICO and AIA in September of 2008 that were as high as the amount of money that AIG ultimately recovered from those two entities?
A. I can't remember.
Q. You used various unsecured debt yields and CDS spreads in terms of analyzing the extent to which AIG was a risky borrower, correct?
A. That's correct.
Q. And is it your understanding that, in general, unsecured debt has a higher yield than secured debt?

A. Correct, yes.

Q. And you understood that the security that the Government got for the revolving credit facility was security that was very important to the Government, correct?

A. I'm not quite sure what you mean, "important to the Government."

Q. The Government was very keen on having collateral for the RCF.

A. Yes.

Q. The Government believed that having the collateral that it had for the RCF made it much more likely that it would get repaid than if it did not have collateral, correct?

A. That's correct.

Q. Now, with respect to the bond yields and the CDS spreads, those reflected, in part, an assessment of the market of credit risk. Is that true?

A. That's true, yes.

Q. They also reflected, in part, an assessment of the market of liquidity risk or liquidity premium, correct?

A. That's potentially true, yes.

Q. Not only is it potentially true, but that was particularly true during the economic crisis of 2007 to

2009, correct?

A. Well, the CDS five-year spread is the most liquid instrument of the CDS market. So, if there was any liquidity premium or discount, it would be small.

Q. Let me ask you -- I think we ought to hand out our book. I was hoping to avoid it, but -- Your Honor, sorry. The problem with these books is they're always prepared in advance. So, we put into it everything we think we might want to use.

THE COURT: I think cross examination has just completed.

MR. BOIES: It would be fair.

BY MR. BOIES:

Q. Let me ask you to turn to Plaintiffs' Trial Exhibit 2161-A and --

A. Do I have them?

Q. Yes.

A. Oh, here. I see.

Q. And what you have there are --

A. 21?

Q. 2161-A, but before you do that --

A. Yeah.

Q. -- let me just explain what you have there, because what you have there are a series of documents and excerpts from documents, because the documents are so voluminous that we only give you excerpts.

A. Um-hum.

Q. However, if at any point in time you want to see the entire document, we have the entire document here in court, and we'll be happy to furnish it to you.

A. Um-hum.

Q. But the first one I want --

A. 2161-A?

Q. Yes.

A. Yes, I have it.

Q. Yes. And this is an excerpt from a book that you coauthored. Is that correct?

A. That's correct.

Q. And let me ask you to look at page 112.

A. Page 112?

Q. Yes.

And, Your Honor, with the Court's permission, I will hand up for the Court and for the witness -- I don't have copies for everybody --

A. I don't have 112.

Q. -- just the book itself, which may be easier to -- also, as an author, I know that --

A. Well, I am very glad you bought my book.

Q. -- that everybody appreciates that.

A. Three copies, so I'll check my royalty

statement. Thanks.
Q. And I would like to direct your attention to page 112 of your book.
A. In this book? Which book now? This book?
Q. Yes.
A. Yeah.
Q. And do you see in the middle paragraph --
A. Yes.
Q. -- you say, "The importance of liquidity to investors becomes apparent in its absence. During the economic crisis of 2007 to 2009, financial markets throughout the world shut down"?
A. Yes.
Q. And you believe that, correct, sir?
A. Yes. Those were very difficult times in the financial markets. There was a credit crunch around this time.
Q. And you say, "Liquidity became an ever more important consideration for investors and the price of liquidity (the liquidity risk premium) soared, as shown in Figure 5.6." Do you see that?
A. Yes.
Q. And that's accurate, correct?
A. Yes. It's showing the difference between the LIBOR rate and I think the Fed funds rate or what was

called the overnight index swap rate, which is the Fed funds rate, forward-looking.

Q. And you then go on to say, "During the last months of 2008 (the third phase of the crisis) the spread between LIBOR and the overnight index swap (OIS) rate soared from its historical level of about 10 basis points to more than 300 basis points, as investors demanded a high-risk premium for even the slightest amounts of illiquidity."

A. Yes.

Q. And you then go on to say, "These spreads are built into bond yields, thereby complicating the decomposition of spreads into a measure of credit risk. That is, the considerable noise in bond prices, as well as investors' preferences for liquidity, suggest that there is a liquidity premium built into bond spreads. Thus, if risky bond yields are decomposed into the riskless rate plus the credit spread only, the estimate of credit risk exposure will be biased upward."

Do you see that?

A. Yes.

Q. And that's what you believe, correct, sir?

A. Yes.

Q. Now --

A. Can I put this down now?

Q. Yes. We will come back to it, but yes, for now.

Let me ask you to look at Plaintiffs' Trial Exhibit 119, and this is already in evidence. My first question is --

A. Let me see, 119.

Q. And my first question is whether this is a document that you relied on in your work.

A. I saw many documents from the Federal Reserve, probably hundreds. I may well have seen this one.

Q. Let me -- let me direct your attention to the email that was sent from Michael Holscher to Meg McConnell, September 17th, 2008, at 3:31 p.m. Do you see that?

A. Yes.

Q. And you know who Meg McConnell is, correct?

A. Yes. She's an executive at Federal Reserve Bank of New York, working with, I think, Tim Geithner.

Q. And do you know who Michael Holscher is?

A. Offhand, I can't remember.

Q. Do you know who Bill Dudley is?

A. Bill Dudley, yes.

Q. Who is he?

A. He is now the president of the Federal Reserve Bank of New York.

Q. And if you go to the second sentence here, it says, "Basically, we took almost no credit risk in extending a loan equal to about 8% of the total assets, which is secured by a senior claim on 100 percent of the assets. Nonetheless, we extended the loan at an exceptional high penalty rate..."

Do you see that?

A. Yes.

Q. Do you recall being aware of this view at the Federal Reserve Bank of New York as of September 17th, 2008?

A. Well, this is just an opinion of one person, Michael Holscher. I'm not quite sure who he is.

Q. Do you recall being aware of this opinion by this person at the Federal Reserve Bank of New York as of September 17th, 2008?

A. As I say, I saw hundreds of documents from the Federal Reserve, emails going back and forth. I don't remember this one. And I don't know who Michael Holscher is.

Q. Now, one of the things that you did say that you relied on were certain notes taken by Meg McConnell. Am I right about that?

A. That's correct, yes.

Q. And that was Trial Exhibit 371. Am I right about that?

A. Am I to look back at my demonstratives or here?
Q. You cited it in your --
A. Yeah.
Q. -- I think --
A. Three-something.
Q. -- Defendant's Exhibit 2738. Defendant's Exhibit 375, I think it is.
A. Which one do you want me --
Q. Do you see your demonstrative, Defendant's Exhibit 2738?
A. Three --
Q. Your demonstrative in your book.
A. Yeah.
Q. Defendant's Exhibit 2738 --
A. Okay.
Q. -- in which you're talking about repayment risk.
A. Yes, that's right. This is handwritten notes of Margaret McConnell during a meeting at the Federal Reserve Bank of New York.
Q. Right. Now, you quote here a statement that says "significant risk that you won't recover principal and interest on this loan." Do you see that?
A. Yes.
Q. First, let me just ask you, how did you happen to come across Defendant's Exhibit 375?

A. It was shown to me by counsel.
Q. Which counsel?
A. I -- my counsel, the Department of Justice.
Q. Did they tell you anything at all about what Ms. McConnell had said about this note?
A. No.
Q. Do you have any understanding as to who made this statement?
A. No. She was just taking notes of the meeting, as I understand it, and this was a comment that was made at the meeting.
Q. And did you investigate who made the comment?
A. There was nothing in the document to indicate who made the comment.
Q. Did you investigate whether Ms. McConnell had said whether this even related to AIG?
A. No. It was just a note in a -- in the minutes of a meeting she was taking, with Geithner and other members of the Federal Reserve.
Q. Well, there wasn't just Geithner and other members of the Federal Reserve. There were a lot of people present at that meeting, correct?
A. I don't know.
Q. You didn't investigate that?
A. No.

Q. So, you don't know who said this, correct?
A. No, I don't.
Q. Or under what circumstances?
A. No.
Q. Or what they were referring to?
A. That they wouldn't recover principal and interest on the loan.
Q. Other than reading this, you don't know anything about the circumstances of this or who said it or on what basis, right?
A. No, I don't know who said it.
Q. Or on what basis, correct?
A. Well, they're talking about the risk of the loan.
Q. When you say "the loan" --
A. Sorry?
Q. When you say "the loan," do you know that this relates even to the AIG loan?
A. I believe so, yes.
Q. Why do you believe that?
A. Because it was concerning the AIG loan.
Q. You mean the discussion was?
A. Yes.
Q. Part of the discussion or all of the discussion?
A. I didn't see all of the discussion.

Q. You didn't see all of the discussion?
A. No.
Q. And did you -- did you actually review all of the handwritten notes of Ms. McConnell?
A. I might have perused them, but I don't remember all of the comments.
Q. While we're on Defendant's Exhibit 2738, right above your quotation from these notes, you make the statement (as read): "Time was needed for asset sales to recover because ex-ante the 'hole [was] too big to be filled...'"
Do you see that?
A. Yes.
MR. ROBERSON: Objection. I think he misread the statement.
THE COURT: I'm sorry?
MR. ROBERSON: I think he misread the statement.
THE COURT: Oh. Do you want him to read it again? Why don't we do that.
BY MR. BOIES:
Q. "Time was needed for asset sales" --
A. No, values.
Q. -- "asset values to recover because ex-ante the 'hole [was] too big to be filled... '" Do you see that?
A. Yes.

Q. Now, what was the date of the statement that the "hole [was] too big to be filled..."?

A. This is a comment, I think, from James Lee, who was -- originally from James Lee, who was the person in charge of the attempt to syndicate the private loan, and then --

Q. Yes.

A. -- there was a comment passed on by somebody at the Federal Reserve, whose name I remembered two hours ago and I forget now, who -- who sort of repeated this in -- it was like a two-line email.

Q. And you knew that what Mr. Lee was referring to was whether the "hole" could be filled by the private sector as of September 15th or 16th, correct?

A. Well, I would say he was looking at the difference between a syndicated loan amount, which was to the private sector 75 billion, and a valuation of the underlying collateral that had been made on the same day, which was, I think, between 49 and 72 billion.

Q. My question, sir, was that you knew what Mr. Lee was referred to was whether the "hole" could be filled by the private sector as of September 15th or 16th, correct?

A. Yes. By private sector loan, yes.

Q. And did you have an understanding as to the effect of the Lehman failure on the ability of the private sector to come up with a financial solution for AIG?

A. You mean a syndicated loan?

Q. A syndicated loan or any other financial solution.

A. Well, I think that the last opportunity was a syndicated loan, and they felt the hole was too big to be filled to persuade other -- other banks, and I think they were seeking out 15 banks or so to take $5 billion slots into the syndicate, and they didn't really find anybody very interested, again, because -- yes, you're right, liquidity was constrained at the time.

Q. And I think you said that you had read the trial testimony of a few people, correct?

A. Um-hum.

Q. Was one of those people Mr. Baxter?

A. No.

Q. Was one of those people Mr. Alvarez?

A. No.

Q. From anything that you have come across, are you aware of Mr. Baxter or Mr. Alvarez saying they believed there would have been a private sector solution except for the Lehman failure?

A. No, I don't remember that.

Q. Are you aware of anyone at the Federal Reserve expressing that view?

A. Not that I recall, no.

Q. Now, back on the -- the question of the riskiness of the loan, if you turn to Defendant's Exhibit 2737, where you first say on that page that the collateral pledged to secure the loan was primarily composed of AIG's illiquid equity interests --

A. Yes.

Q. -- in its insurance subsidiaries. Do you see that?

A. Yes.

Q. Do you know what the value was of the assets other than stock in AIG's insurance subsidiaries --

A. I can't say --

Q. -- that was pledged to secure the loan?

A. I can't remember. As I say, "primarily composed."

Q. When you say "primarily," can you be a little more specific than that? I assume "primarily" means at least 51 percent, correct?

A. The majority.

Q. The majority.

Can you be any more specific than simply saying a majority of the assets?

A. No. I think the -- the majority of the assets were the equity interests in the insurance subsidiaries.

Q. Now, you say that the value of the equity interests pledged to secure the loan were nearly perfectly correlated with the likelihood of AIG's default.

A. Yes.

Q. And you said that if the insurance companies were in trouble, then AIG would be in trouble. Do you recall that?

A. Yes, the correlation.

Q. Now, this would -- this would be the case for the stock, in your view, related to the AIG insurance subsidiaries but would not be true for assets like repo collateral and cash and other securities, correct?

A. Well, tradable securities that have a market value as of that time, such as repo collateral, that's correct.

Q. You also said that if AIG is in trouble, then the insurance subsidiaries might be seized. Do you recall that?

A. Yes. To protect policyholders, yeah.

Q. Now, are you aware of instances in which insurance holding companies have gone into bankruptcy without the seizure of their insurance subsidiaries?

A. I don't know of every single insurance holding company bankruptcy and how often they are seized, but I know that they are commonly seized.

Q. They are commonly seized?

A. They are commonly seized in terms of conservatorship. The insurance regulator comes in and takes possession of the conservatorship.

Q. Can you tell me what instances you're familiar with where a holding company went into bankruptcy and operating insurance subsidiaries were seized?

A. Well, there's a paper there on my document list, academic paper, that discusses the commonality of this occurring. So, I'm relying on that.

Q. But can you give me any example as you sit here?

A. It has hundreds of examples of insurance companies going into bankruptcy.

Q. Insurance companies, yes.

A. Holding companies.

Q. Well, that's what I'm trying to distinguish.

A. Oh, are you asking about holding companies versus companies?

Q. Yes. Yes, you see, because --

A. Yes, okay. So, you are making a distinction between a holding company and a company.

Q. And you understand why I'm making this distinction.

A. Yes, because a company that's owned can't go in bankruptcy if it's a holding company.

Q. Right. And if you have an insurance company that is insolvent, it can be -- go into conservatorship, rehabilitation, a variety of things, right?

A. Yes.

Q. But what was at issue with respect to AIG is you had a holding company --

A. That's correct.

Q. -- and the concern was the holding company would get into trouble --

A. Yes.

Q. -- and that might somehow affect the operating subsidiaries, correct?

A. We were concerned about the operating subsidiaries, yes, to make policyholders safe.

Q. Now, that's why I asked you the question, are you aware of any instances in which a holding company has gotten into trouble, gone into bankruptcy, and that has caused the seizure of -- not of the holding company, but of the operating subsidiaries?

A. You mean for insurance companies, not banks. You mean for insurance companies rather than bank holding companies. You're talking about insurance holding companies.

Q. Yes, a company -- a holding company that owns insurance companies.

A. I understand what you're saying, but I'm just saying -- I just want to define the question. I can't give you an example of one.

Q. Are you aware of a company called Conseco?

A. Yes.

Q. And Conseco went into bankruptcy, correct?

A. I believe so, ten years ago or something like that.

Q. And Conseco owned insurance companies, correct?

A. I believe so. I'm not 100 percent sure, but I believe so, yes.

Q. And the Conseco insurance subsidiaries were not seized, correct?

A. I don't know.

Q. Now, let me ask you to look at Plaintiffs' Exhibit 1553, which I need to hand out. This is a Federal Reserve document that is already in evidence.

A. 1553.

Q. I'm handing it out.

A. Ah, okay.

Q. And this is a restricted Federal Reserve document representing the minutes of a conference call concerning the Federal Reserve Bank of New York, Bank Supervision, the Legal Department, the purpose of which is stated to be "AIG contingency planning and legal/regulatory framework."

Do you see that?

A. Yes.

Q. And the first question is (as read): "If the holding company files for bankruptcy, what would be the New York State Insurance Department's approach?" And the response is, "Solid property and casualty companies with sufficient capital which would be walled off from the insolvency proceedings. The companies can continue to run, plenty of money to pay claims since the New York State Insurance Department feels comfortable with the current level of surplus."

Do you see that?

A. Yes.

Q. And is that consistent with your understanding?

A. Well, that's what the document says. I haven't seen this document, as far as I can recall.

Q. Counsel didn't show you this document?

A. I don't remember seeing this document.

Q. And if you turn to the second page, there's a heading that says, "Bankruptcy of Parent v. Receivership of Insurance Entities."

A. Can I just finish reading this?

Q. When you've finished, let me know.

A. So, this has nothing to do with New York. It has to do with Texas.

Q. When you're finished, let me know.

A. Yes, okay. Let me -- let me read through it, then. (Document review.)

Q. Are you finished?

A. Yes.

Q. Okay. Now, on the second page at the top, do you see where the heading says, "Bankruptcy of Parent v. Receivership of Insurance Entities"?

A. Yes.

Q. And it says, "If parent files for bankruptcy, it does not force the insurance regulators to do anything as long as the insurance subsidiaries remain financially healthy and solvent."

A. Yes.

Q. "However, New York State Insurance Department would increase monitoring of the AIG parent to make sure that there aren't inappropriate transfers out of the subs. Article 74, however, does not have any provision that forces the department to come in and seize the institution but there are a number of situations where they are empowered to do that."

Do you see that?
A. Yes.
Q. And is that consistent with your understanding? I understand you said that you hadn't seen the document.
A. And the next first sentence of the next -- it says exactly what I said before, that --
Q. Can I get you to focus, sir, on my question?
A. Yes.
Q. Okay. I understand you have got a lot of things you want to say --
A. No, I'm just saying if you read the next sentence in the second paragraph.
Q. If you just let me ask the question --
A. Yes.
Q. -- respond to the question, and we are going to go through this whole document, okay?
A. Yes, okay, that's great.
Q. So, first, is what we just read consistent with your understanding?
A. There's options to the regulators -- the insurance regulators to take various actions, correct.
Q. Okay, right. And if the New York State Insurance Department determines that a company is hazardous to its policyholders and/or is insolvent, it could seek the insurer -- the consent of the insurer to

rehabilitation. Do you see that?
A. Yes.
Q. And the insurer can either give its consent or not give its consent, correct?
A. That's correct.
Q. And if it doesn't give its consent, then the issue would have to go before a judge, correct?
A. That is what it says.
Q. And you don't have any reason to doubt it, correct?
A. No.
Q. Now, you said something while you were perusing the document about it not relating to Texas or something like that.
A. Well, I was just looking at the other side. It says that if Texas entities have a shortfall, the Texas regulators would have to choose to intervene. There is nothing that the NYSID could do.
Q. And did you investigate what the view was of the Texas regulators?
A. No. I'm just reading what it says here.
Q. I'm asking you, sir --
A. No, I did not.
Q. -- whether as part of your analysis and investigation, you looked at what the view was of the

Texas regulators.
A. No.
Q. Other than my showing you this today, did you look at what the view was of the New York State Insurance Department?
A. I was unaware of this document.
Q. Other than this document, did you investigate what the view was of the New York State Insurance Department with respect to what would happen to the AIG insurance subsidiaries if the parent went into bankruptcy?
A. I don't remember seeing any specific documents that would deal with that.
Q. Okay. Let me turn to your chart or your charts 2728 and 2729.
A. 2728?
Q. And 2729. And these are charts in which you try to illustrate your opinion that there was excess liquidity trapped at the insurance subsidiary level that could not be used. Do you recall that?
A. Upstreamed, yes. Yes.
Q. And I think they showed you a -- a document that had been prepared by one of our experts. Do you recall that?
A. Mr. -- Dr. Cragg. Sorry.

Q. And do you still have that up there with you? It was Plaintiffs' Trial Exhibit 5354.
A. It doesn't seem to be -- oh, okay, it may be here. Yeah.
Q. And with respect to your Exhibit 2728, you took Dr. Cragg's calculation of excess liquidity from Plaintiffs' Trial Exhibit 5354. That was your starting point, correct?
A. Yes.
Q. And then you attempted to set out how much of that excess liquidity could be made available to the parent, correct?
A. Well, AIG, AIGFP, or AIGSL or interaffiliate loans among the insurance companies, basically restrictions on affiliate transactions.
Q. Now, going back to Plaintiffs' Trial Exhibit 5354.
A. Yes.
Q. This shows the assets that each of these 13 subsidiaries had that would qualify for a PDCF loan if they had access to the PDCF, correct?
A. If each of these 13 had individual access, yes.
Q. Right. And then next to it, it shows the securities lending loan balance owed to counterparties for each of those subsidiaries, correct?

A. That is correct.

Q. And then the difference between those two is what you start out with on your chart 2728, correct?

A. The yellow bars, yes.

Q. Now, did you understand that the insurance subsidiaries shown on Plaintiffs' Trial Exhibit 5354 were each subsidiaries that themselves had securities lending balances?

A. Except for number 6.

Q. I --

A. Oh, 6 does have --

Q. I think 6 has --

A. -- a minimal amount.

Q. -- a very minimal amount, and 4 has a very minimal amount, and 7 has enough so that you can see it a little bit better, but it's still pretty small.

But each of these companies had to come up with liquidity to deal with those balances, correct?

A. That's correct, yeah.

Q. And did you understand that in order to provide liquidity to these insurance subsidiaries, AIG, the parent, was, in September of 2008, putting money into those subsidiaries?

A. I believe so, yes.

Q. And if the subsidiaries had been able to solve their own liquidity problem, that would have eliminated the need for AIG, the parent, to put money into them, correct?

A. Are you saying -- can I just ask you a question? Are you saying each of the 13 here would be able to go to the Federal Reserve Bank of New York and ask to be a primary dealer?

Q. I haven't -- I haven't asked that --

A. Because that's my interpretation of what you're saying.

Q. -- I haven't remotely gotten there yet. My --

A. I guess I'm ahead of you.

Q. Well, yeah, I think you are, and I understand that you may think you know where I'm going with this and not --

A. Well, perhaps not.

Q. -- want me to get there, but what I would like you to do is just focus on my steps.

A. Okay.

Q. Okay? And you understood that if the AIG insurance subsidiaries had been able to solve their own liquidity problems arising from the securities lending programs, that that would have reduced the liquidity drain on AIG, the parent, correct?

A. If they could have upstreamed the --

Q. No, upstream means taking money from the subs to the parent, correct?
A. Yes.
Q. But you understood that what was happening in September of 2008 was that in order to meet the liquidity needs of the insurance subsidiaries, AIG, the parent, was putting money into the insurance subsidiaries.
A. Yes. Only about 12 billion, though.
Q. And that would be called downstreaming, correct?
A. Yes, correct. About 12 billion.
Q. And in addition to the 12 billion that AIG had already put into the insurance subsidiaries, going forward, it was projected that there would be additional amounts that were required, correct?
A. You mean required from AIG?
Q. AIG, the parent.
A. Yeah.
Q. And, in fact, do you know how much of the $37 billion that was borrowed by AIG, the parent, from the Federal Reserve during those first few days went into insurance subsidiaries to deal with the securities lending issues?
A. No.
Q. Approximately?

A. No.
Q. You know there was some amount, correct?
A. I believe there was some, but I don't know how much.
Q. And you never investigated how much?
A. No.
Q. And if the insurance subsidiaries had been able to provide their own liquidity, then AIG, the parent, would not have had to put in the $12 billion and would not have had to put in whatever additional amount of money they put in on or after September 16th, correct?
A. If each, on an individual basis, could solve their liquidity problems, yes.
Q. And if the individual insurance companies could each have accessed a credit facility comparable to the PDCF, that is, a credit facility that would take PDCF collateral and provide liquidity for it --
A. This is a new facility now? You've invented one?
Q. I have not invented one.
A. I thought the acronym here was PDCF access.
Q. That's right.
A. You have to become a primary dealer.
Q. My question to you, sir, my question to you is that you know that each of these insurance subsidiaries

had collateral that if they had had access to the PDCF would have resulted in liquidity, correct?

A. Yeah, but it --

Q. No, but that's just a question --

A. -- they have to fulfill the criteria --

Q. There is no "but" here. That's yes or no.

A. No, they did not have access, because they did not have the criteria on capital or trading --

MR. BOIES: Your Honor, Your Honor --

THE WITNESS: -- or auctions.

THE COURT: Once again, sir, please just answer the question.

THE WITNESS: I'm sorry, yeah.

BY MR. BOIES:

Q. You know that each of these insurance companies -- individual insurance companies had collateral that was of the type that primary dealers brought to the PDCF and in return received liquidity.

A. Yes.

Q. Okay. And each of these insurance subsidiaries had enough of that collateral that if they had been able to exchange that collateral for liquidity, it would have solved their securities lending problem, correct?

A. But how would they have been able to post it? Not as a PDCF, because they did not have the criteria to become a --

MR. BOIES: Your Honor --

THE COURT: Sir.

THE WITNESS: I'm sorry.

THE COURT: The question?

BY MR. BOIES:

Q. You knew that each of these AIG insurance subsidiaries had enough of that PDCF-eligible collateral, that if they had been able to exchange that collateral for liquidity, that would have solved their securities lending problem, correct?

A. If they had some new centralized system, possibly, yes.

Q. It's not possibly, sir, and it's not some new system. This is a simple question.

You knew that each of these AIG insurance subsidiaries had PDCF-eligible collateral, correct?

A. Correct.

Q. And you knew they had enough of that collateral that if they had been able to exchange it for liquidity, that would have solved their securities lending problem, correct?

A. Each single one?

Q. Yes.

A. Individually?

Q. Yes.
A. Yes.
Q. Okay. Now, let me turn now to another subject. I'm reminded that I asked you something about Texas, and I think I know the answer to this question, but I will -- I will ask it anyway.
Would you look at Plaintiffs' Trial Exhibit 628.
A. Is that one we just looked at?
Q. No, this is a new one that I'll hand up, and I think it will be very short. And my question is really just whether this is a document that you reviewed in connection with any of the work that you were doing.
A. I think, yeah, at the beginning of the whole process, probably a year or so ago, I did see this. It's from the GAO, some interviews.
Q. And is this something that you relied on, including for the issue of what would happen to insurance subsidiaries in the event of a parent company bankruptcy?
A. I don't remember what it says, so I suppose we can read it again.
Q. Without taking the time to read it, do you recall that this was a document that you relied on for the substance of it?
A. No. I read it. I don't remember if I relied on

it or not.
Q. Okay. Then take your time to tell me whether or not you relied on it.
A. (Document review.) Do you want me to read the whole thing or --
Q. No, just enough to be able to tell me whether this is something you relied on.
A. Yeah, I remember reading it.
Q. And was it something that, in addition to reading, you relied on in forming your views?
A. Well, this says that the insurance regulators could intervene if they felt the need to.
Q. All I'm asking, sir -- I'm not asking you to read the document out loud.
A. I'm giving you a synopsis.
Q. And I'm not even asking for a synopsis. What I'm asking is simply whether this was a document that you relied on in forming your views.
A. I read it. It tells me --
Q. You told me that you read it, and I take it there are a number of things that you read that you didn't rely on, correct?
A. Yes.
Q. Okay. And what I'm trying to do now is find out whether, in addition to being a document that you read,

it was a document that you relied on.

A. Not explicitly, no.

Q. Did you rely on it implicitly?

A. I don't know.

Q. Okay. We spoke a moment ago about PDCF-eligible collateral. You were aware that in the 2007-2009 financial crisis, the Federal Reserve began to accept relatively low-quality assets?

A. Through what facility do you have in mind?

Q. Well, let me ask you to look at Plaintiffs' Trial Exhibit 3139, and this is a document that you recognize, correct, sir?

A. Yes.

Q. And this is an expert report that you submitted in an arbitration. Is that correct?

A. It's the High Court of Justice. It concerned a dispute, yes, between JSC bank and a former, I think, owner of JSC bank.

Q. Um-hum. And do you see the last sentence in your paragraph 20 that appears on page 15 of the exhibit?

A. Yes, I do.

Q. Where it says, "The Fed sought to actively ameliorate banks' liquidity shortages by accepting relatively low-quality assets, including commercial loans, as collateral, subject to a haircut on the asset's face value."

A. That's correct, yes.

Q. And that was accurate, correct, sir?

A. Yes, although they did accept equity eventually, for example, for PDCF in September 2008. They had always accepted commercial loans, but some of the commercial loans were of poor collateral values as of this time because of the crisis. So, they had always accepted commercial loans.

Q. You mentioned the PDCF in September, and I take it what you're referring to is on Sunday, September 14th, 2008, the Federal Reserve expanded the types of eligible PDCF collateral to include all types of collateral used in the repo market, including noninvestment grade securities and equities, correct?

A. Yes.

Q. Now, just staying -- since we're at your expert report that's marked as Plaintiffs' Trial Exhibit 3139, at the top of the page, you write, "When financial markets cease functioning, the Government is left as the ultimate provider of liquidity and credit to the economy."

Do you see that?

A. Yes.

Q. And that's something you believe, correct?
A. Yes, lender of last resort.
Q. As of September 19th, 2008, do you know about how much of the collateral pledged at the PDCF was equity?
A. No, I don't remember.
Q. Would approximately 40 percent sound right?
A. I can't remember.
Q. Let me ask you to look at Plaintiffs' Trial Exhibit 293, which is already in evidence.
A. 293? 293, and here I am in the thousands. Yeah, got it.
Q. And is this a document that you've seen before?
A. I suppose I'm looking at the wrong thing, because there's nothing about collateral on here as far as I can see.
Q. You've got Plaintiffs' Trial Exhibit 293?
A. Okay, perhaps you can tell me what I should be looking at.
Q. My first question is simply whether this is a document that you've seen before.
A. No, I don't think so.
Q. Okay.
A. Not that I can remember.
Q. Do you see on page 3, that what is attached to a

cover email is a "Federal Reserve Bank of New York Financial Summary, Statement of Condition and Collateral Summary" --

A. Yes.

Q. -- as of October 10th, 2008?

A. Yes.

Q. And if you turn to page 7 of the exhibit, do you see in the bottom half of the page, on the left-hand side, a table that is headed "Collateral Composition across all PDCF Participating Dealers"?

A. Yes.

Q. And do you see that equity represents 40.47 percent?

A. Yes. Traded equity, not pure equity, just traded in the market.

Q. When you say "traded," it doesn't say "traded" there, right?

A. No, but that's what it was, because it --

Q. Now, you just told me you hadn't seen this document, right?

A. But I know about what equity was accepted in the time period. When it was accepted, it was tradable equity with a low haircut.

Q. Now, when you say traded equity, first of all, this was noninvestment grade equity, correct?

A. There's no such thing as a noninvestment grade equity. You mean debt?
Q. There's no such thing as noninvestment grade equity?
A. I don't think rating agencies rate the equity of companies.
Q. This was equity of companies that had a noninvestment grade rating, correct?
A. Oh, that's a different question. It was still traded.
Q. This is the equity of -- this is the equity of companies that had a noninvestment grade rating, correct?
A. I don't know, because this says "equity."
Q. But you know -- I thought you just told me that you know -- knew what kind of equity they had -- they had taken.
A. Tradable equity, traded in the markets, whether it's just -- whether it's low-rated companies or high-rated companies, it's tradable equity.
Q. Did you -- I think you did say that one of the few people whose trial testimony you looked at was Mr. Bernanke's, correct?
A. Yeah.
Q. Do you remember what Mr. Bernanke testified to

with respect to whether the securities taken by the Federal Reserve in connection with the PDCF had to be tradable?

A. No. I just remember --

Q. Do you remember what he said? That's my question.

A. I can't remember, no. I can't remember.

Q. Do you remember anyone telling you that as long as there was a third-party price, even if there was not a market for the security, it would be taken by the PDCF?

A. No.

Q. I want to be sure I got an answer to the question before. Do you know how much of the equity was the equity of companies with less than investment grade ratings?

A. This is showing debt, then it shows equity as a lump sum, then it shows unknown ratings, so I'm not quite sure what your question is.

Q. My question is, do you know how much of the equity that represents this 40.47 percent of all collateral posted to the PDCF --

A. No. Of -- of --

Q. -- was the equity of companies with less than investment grade ratings?

A. For its bonds, no.

Q. Oh, by the way, the next line down after "Equity," it says "Unknown rating, 23.06%." Do you see that?

A. Yes.

Q. Do you know what that refers to?

A. Nonrated companies who don't issue bonds, or if they do issue bonds, they're not rated. You don't have to be rated.

Q. Um-hum, okay. You testified earlier that you did not do a study of the collateral that AIG posted for its revolving credit facility. Did you, as part of your investigation, review what representatives of the Federal Reserve Bank said about the quality of the AIG collateral?

A. Actually, I think I said that they posted nontraded shares of their insurance subsidiaries.

Q. That wasn't my question, sir. I'm not sure what -- what question did you think you were responding to?

A. I thought you said I said earlier, and I'm just repeating what I said earlier.

Q. Do you remember me asking you earlier about whether you had done a study of the credit quality of the assets that were pledged by AIG? Do you remember me

asking you that question?
A. I thought I said I believed it was mostly illiquid, nontradable equities of subsidiaries.
Q. Let me ask you to look at page 281 of your deposition, sir.
A. Is this in a different book?
Q. I am going to have to hand it up.
A. Do I have it?
Q. Yes.
Could I approach, Your Honor?
THE COURT: Sure.
BY MR. BOIES:
Q. It is this one right here.
A. Okay. Page?
Q. 281, line 5. Do you have it?
A. Yeah.
Q. "QUESTION: Did you do a study as to the credit quality of the assets that were pledged by AIG?
"ANSWER: No."
Do you see that?
A. Yes.
Q. And I take it that was truthful, accurate, and complete testimony at the time you gave it under oath?
A. I know I just stated what they posted, which was illiquid, tradable -- nontradable assets, equity assets

in their subsidiaries. This question seems to be more specific, to drill down even further.

Q. "QUESTION: Did you do a study as to the credit quality of the assets that were pledged by AIG?

"ANSWER: No."

Do you see that?

A. Yes, I do see it.

Q. Okay. And that was your testimony then?

A. I'm just telling you what I looked at, which was the nontradable assets.

Q. And you knew at the time that you gave this deposition you were under oath, correct?

A. That's correct.

Q. And you knew that that oath was to tell the truth, the whole truth, and nothing but the truth?

A. Yes, I did.

Q. Now, going back to my earlier question, did you, as part of your investigation, review what representatives of the Federal Reserve Bank said about the quality of the AIG collateral?

A. No, I cannot remember that.

Q. Just to be clear, when you say you can't remember, do you mean you can't remember whether you did it?

A. I didn't do any comparable analysis of calculations of value.

Q. In addition to not doing any comparable analysis of calculations of value, did you not investigate what Federal Reserve personnel said about the quality of the AIG collateral?

A. What do you mean, in terms of -- what do you mean by "quality"? Perhaps we can define "quality" for me. It's not debt, so it's -- we're talking about equity of subsidiaries. I'm not quite sure what you mean by collateral quality.

Q. You understand that AIG posted collateral for the revolving credit facility, correct?

A. Yes.

Q. And you understand that that collateral had to be acceptable to the Federal Reserve Bank of New York, correct?

A. Correct, yes.

Q. Did you investigate or analyze what the Federal Reserve Bank of New York personnel said about the quality of the collateral that AIG posted?

A. I can't remember.

Q. Do you recall -- you know who Mr. Geithner is, of course.

A. Yes.

Q. Do you recall Mr. Geithner saying, in words or in substance, that AIG had enough high-quality collateral to permit the Federal Reserve to extend a loan sufficient to stabilize the firm?

A. I don't know if he said it specifically, but he said it was secured to the satisfaction of the Federal Reserve. But there was other people who said it was -- the collateral was --

Q. Do you understand what the question is?

A. Yes, I do understand the question.

Q. What was the question?

A. You can repeat it to me.

Q. But do you remember the question?

A. Please repeat it to me.

Q. But do you remember the question?

A. No, I don't.

Q. Okay.

A. Please repeat it.

Q. Okay. And if at any time in the course of an answer you find that you don't remember what the question is, if you simply let me know, I'll repeat it, okay?

A. Okay, thank you.

Q. Do you recall Mr. Geithner saying, in words or in substance, that AIG had enough high-quality collateral to permit the Federal Reserve to extend a loan sufficient to stabilize the firm?

A. In those exact --

Q. That's a yes or no or I don't remember.

A. I don't remember.

Q. Okay. Let me ask you to look at Plaintiffs' Trial Exhibit 2206.

Your Honor, I would offer this limited to the statement by -- statements by Mr. Geithner. I would be prepared to offer the entire document if counsel for the Government would like me to, but for my purposes, I just need Mr. Geithner's --

A. Are we talking about a DX document, sir, or PX document or JX?

Q. PTX. PTX 2206.

MR. ROBERSON: Object on hearsay. Mr. Geithner is not here. It is a hearsay document, plain and simple.

THE WITNESS: Yes, I've got it.

THE COURT: So, you don't want any of it to come in?

MR. ROBERSON: Correct.

THE COURT: I am going to admit it as to the statements of Mr. Geithner.

(Plaintiffs' Exhibit Number 2206 was admitted into evidence.)

THE WITNESS: PTX -- what number? Sorry.

BY MR. BOIES:

Q. PTX 2206. I am going to go to page 172 of the hearings, but it's page 176 of the exhibit. Page 176 of 232.

A. So, PTX 2206?

Q. Yes, sir.

A. And what page?

Q. Page 176 of 232.

A. Okay, yes.

Q. And the third-to-last paragraph says, "Some have asked why Lehman went bankrupt while AIG received extraordinary assistance that prevented default. The answer is that AIG presented a very different case. AIG had enough high-quality collateral to permit the Federal Reserve to extend a loan sufficient to stabilize the firm -- largely the profitable insurance businesses that were relatively insulated from the firm's losses on complex financial transactions."

Do you see that?

A. Yes.

Q. And does that refresh your recollection as to whether you were aware of Mr. Geithner holding these views?

A. Well, I know that he -- his view was it was

secured to the satisfaction of the Federal Reserve.
Q. That's not what he says here, of course.
A. No.
Q. And my question is, are you aware of him having the views that he expresses here?
A. No.
Q. Okay. Now, you're not an expert in Section 13(3) lending, correct?
A. No.
Q. In the course of your work, you are, however, familiar with Federal Reserve lending pursuant to 13(3), are you?
A. The criteria.
Q. Yes.
A. The basic criteria.
Q. The basic criteria.
Is that something that you learned for purposes of this case or was that something that you were familiar with before?
A. No. Actually, I learned it back to front from reading Dodd-Frank, which eliminated 13(3).
Q. With respect to 13(3), did you understand that it was necessary for the Board of Governors to review and determine the discount rate to be applied?
A. Well, I think they had to approve by at least

five votes the transaction.
Q. And in your understanding, did the transaction, as you used that word, include the discount rate to be applied?
A. You mean the loan rate?
Q. Yes.
A. Well, you used the term "discount rate." The discount rate -- you mean the loan rate, the rate on the loan?
Q. Yes. I -- that's what I mean.
A. I'm trying to understand. I've never heard it called a discount rate before.
Q. You've never heard it called a discount rate?
A. Not for this loan, no. I've just heard of it as being a loan rate.
Q. Okay. Do you recall that Section 13 -- have you ever read Section 13(3)?
A. Yeah. I read through the section once.
Q. And did you see a reference to a discount rate there?
A. I can't remember. I'm using common parlance, perhaps.
Q. But whether you call it a discount rate or a rate or a loan rate or an interest rate, whatever you call it, did you understand that under 13(3) the Board

of Governors had to review and determine that rate?

MR. ROBERSON: Objection, Your Honor, on two grounds. One, obviously, it calls for a legal conclusion. Secondly, he just testified a moment ago he's not an expert on 13(3) lending.

THE COURT: Well, for what it may be worth, I'll take his understanding.

MR. ROBERSON: Thank you, Your Honor.

THE WITNESS: I'm sorry. What was the question?

BY MR. BOIES:

Q. Sure. And if you don't have any understanding, that's fine, but if you do have an understanding, I want to know it.

Did you understand that under 13(3), the Board of Governors had to review and determine the loan rate or interest rate or discount rate?

A. All I know is that they had to approve the loan that was made by a Federal Reserve district, such as the Federal Reserve Bank of New York.

Q. Okay. As part of your analysis and investigation, did you examine what the Board of Governors approved with respect to the AIG credit facility?

A. Well, they approved it.

Q. Did you analyze or investigate what they

approved?
A. They approved the term sheet.
Q. They approved the term sheet for the revolving credit facility?
A. Correct.
Q. And did you get that understanding from reading the minutes of the Board of Governors meeting?
A. I didn't read the minutes, no.
Q. What is the source of your understanding that the Board of Governors approved the term sheet for the revolving credit facility?
A. That they voted five-zero in favor of the loan going ahead.
Q. And how did you learn that?
A. I can't remember.
Q. Was that something that was told to you by counsel for the Government?
A. No. I might have read it somewhere.
Q. Let me turn to another subject. You testified on direct examination, with respect to the exchange for E and F preferred stock, that the exchange occurred at $45, which was higher than the market price. Do you recall that?
A. I believe so, yes.
Q. Now, when you say the exchange occurred at $45,

am I correct that what you mean is $45 was divided into the liquidation preference and that resulted in the number of common shares that were provided to the Government in exchange for the E and F preferred?

A. That's correct. So, they got fewer shares than if they had divided by $40.

Q. Because the higher the number that's being divided into the liquidation preference, the fewer shares come out.

A. That is absolutely correct.

Q. Now, let me go back to my demonstrative, Plaintiffs' Trial Exhibit 5403, and we were talking about the Series C, E, and F exchange that took place on January 14th, 2011.

A. Yes.

Q. What was the AIG stock price on January 14th, 2011?

A. I can't remember exactly, but I believe it was around $40. Around $40.

Q. Around $40? You've got that in your report. You have the stock prices, don't you?

A. I can look in my report. Do you want me to look at it?

Q. Yes.

MR. DINTZER: Your Honor, I don't mean to interrupt at all, but since he's looking, I just was wondering, could we save a few minutes at the end to discuss the proffer sheet? I apologize, Counsel, for interrupting, but to just sort of put a bookmark in that I neglected to do earlier. The Court suggested that we may --

THE COURT: Maybe we should do it now and we can do this tomorrow. Is that all right?

MR. DINTZER: I didn't mean to interrupt counsel's questioning.

MR. BOIES: That's fine. That's okay.

THE COURT: All right.

Professor Saunders, you can take your report and go out in the lobby, if you wish.

THE WITNESS: Am I coming back?

THE COURT: No, we will pick up again tomorrow morning.

(Witness excused.)

THE COURT: Yes, Mr. Dintzer.

MR. DINTZER: Yes, Your Honor. I mean, I'd be happy to go through each of these numbered items, but my understanding was -- and perhaps I misunderstood -- but that the Court was going to take a look at the topics so that we could --

THE COURT: I did spend a few minutes with that up in chambers, and in going through the list, I think the items I identified this morning, which I think were items 3 and 4, those are the two that I just really feel I don't need to hear more about. The others, you know, I think are fair game if they want to present evidence on it.

MR. DINTZER: Then, Your Honor, we would ask for a detailed proffer by the end of business tomorrow so that we could at least, I mean, have an understanding of what they're going to have their expert testify about so that we can prepare.

MR. BOIES: We will undertake to do that, Your Honor.

THE COURT: Sure.

MR. BOIES: I will make it as detailed as I can, and it will be pretty -- it will reflect the fact that this is going to be short. We've spent more time on this already, I think, than it will probably take to do it, but I will give them -- and maybe -- maybe they will look at it and just stipulate to it, because a lot of this is just going to be filling things in. But I will give them that by the end of the day tomorrow, and, of course, any demonstrative exhibits we have, they will have 48 hours in advance.

THE COURT: How much time do you anticipate with

Professor Daines?

MR. DINTZER: My estimation would be two hours or thereunder.

THE COURT: For direct?

MR. DINTZER: Yes.

THE COURT: Okay.

MR. BOIES: I'm going to try --

THE COURT: And that's the last witness?

MR. DINTZER: That would be our last witness, Your Honor.

MR. BOIES: I will try to compress this.

THE COURT: Okay.

MR. BOIES: The -- and perhaps at the beginning we can tell the witness that if he gives us yes or no answers, we will get him out faster, and we'll be able to move it along.

THE COURT: All right.

MR. DINTZER: Your Honor, I must object to that. I think the witness is answering the question, but separate from that, if Mr. Boies can move this along, we would -- as the Court's already ruled, that they are going to be allowed to provide this testimony, as we had mentioned earlier, the ideal would be that they just come in, bring their expert in tomorrow, we wrap up our case, and they can go ahead and provide it. Then counsel doesn't have to give me a proffer, because we will have the testimony and we will have that for this weekend.

MR. BOIES: I think that's going to be challenging, but we will do the best we can, Your Honor.

THE COURT: We will see how it goes.

MR. DINTZER: Thank you, Your Honor.

THE COURT: All right. We are adjourned until 9:30 tomorrow morning.

(Whereupon, at 4:58 p.m., the proceedings were adjourned.)

CERTIFICATE OF TRANSCRIBER

I, Susanne Bergling, court-approved transcriber, certify that the foregoing is a correct transcription from the official digital sound recording of the proceedings in the above-titled matter.

DATED: 11/21/2014 ________________________________

SUSANNE BERGLING, RMR-CRR-CLR

ADMITTED EXHIBITS

PX	PAGE	DESCRIPTION
1189	8170	AIG Investments Slide Deck - Securities Lending Liquidity Contingency Plans - A Presentation to Steve Bensinger (March 2008)
1502	8168	AIG Draft Slide Deck - Securities Lending Liquidity Contingency Plan (September 5, 2008)
2206	8350	Testimony of Chairman Ben S. Bernanke Before the Committee on Financial Services, U.S. House of Representatives (April 20, 2010)
3228	8287	Email exchange between Mr. Baxter and Mr. Huebner

DX	PAGE	DESCRIPTION
176	8189	AIG FINANCE COMMITTEE PACKAGE
293	8165	EMAIL FROM EDOUARD MORIN TO DAVID JUNIUS RE: ALSO SEND THE FILE YOU JUST BROUGHT DOWN TO JOHN GRACE
363	8196	EMAIL FROM KEVIN WARSH TO DONALD L KOHN RE: AIG, SEPTEMBER 15, 2008, DISCUSSING RECEIVED REPORT ON CAPITAL HOLE AT AIG
375	8197	HANDWRITTEN NOTES OF SEP 16 2008 CALL WITH SECRETARY AND CHAIRMAN, DUPLICATE OF DXX 417

426	8184	EMAIL AND ATTACHMENT BY FERNANDO YANEZ RE: NORTHSTAR UPDATE V7, ATTACHMENT JPM NORTHSTAR UPDATE V7.PPT (JMP AVALUATION OF AIG)
428	8184	EMAIL AND ATTACHMENT FROM S GRIFF NORQUIST TO TIM STAMBAUGH FORWARDING UNDATED PROJECT NORTHSTAR POWERPOINT DECK
550	8215	EMAIL FROM KATHLEEN SHANNON, TO MARC BERNSTEIN AND LIST, CC ANASTASIA KELLY, RE: CREDIT FACILITY, WITH ATTACHMENTS
894	8225	PLAINTIFF'S RESPONSES AND OBJECTIONS TO DEFENDANT'S REQUESTS FOR ADMISSIONS, JANUARY 17, 2014
974	8150	STANDARD & POOR'S GLOBAL CREDIT PORTAL RATINGSDIRECT BULLETIN: AMERICAN INTERNATIONAL GROUP INC. RATINGS UNAFFECTED BY SECOND-QUARTER'S $5.4 BILLION LOSS
976	8196	EMAIL FROM DAN JESTER TO KEVIN WARSH RE: RE: IN FOMC MTG
1308	8166	HTTP://WWW.NEWYORKFED.ORG/MARKETS/PRIDEALERS_POLICIES_920122.HTML
1399	8148	METLIFE JUNE 2008 10-Q
1431	8170	EMAIL FROM PATRICIA MOSSER TO TIMOTHY GEITHNER ET AL RE: AIG MEETING THIS AFTERNOON
1442	8189	EMAIL FROM STEVEN BENSINGER TO ROBERT GENDER, CHRISTOPHER SWIFT RE: UK PAB FREEZE

1443	8187	EMAIL FROM STEVEN BENSINGER TO ROBERT WILLUMSTAD, WILLIAM DOOLEY RE: CP
1615	8156	CAPITAL IQ CDS
1893	8187	EMAIL FROM ROBERT GENDER TO WILLIAM DOOLEY RE: GOLDMAN SACHS AND DISCUSSING BUY-BACK OBLIGATIONS, SEPTEMBER 15, 2008
1894	8187	EMAIL FROM ROBERT GENDER TO KEN HARKINS, ANASTASIA KELLY, KATHLEEN SHANNON, MICHAEL LEAHY, TERI WATSON, CHRISTOPHER SWIFT, KYLE JENNINGS AND CHRIS NIXON. EMAIL RE: AIG AND PA INSURANCE DEPT. GUARANTEES ON DRAWING OF PARTICIPANTS IN THE INTERCOMPANY CREDIT FACILITY, SEPTEMBER 16, 2008
1896	8189	EMAIL FROM ELIAS HABAYEB TO CHRISTOPHER SWIFT, WILLIAM DOOLEY, PATRICIA SKIGEN, ANASTASIA KELLY, BRIAN SCHREIBER AND ROBERT WILLUMSTAD, RE: FW: HONG KONG AND DISCUSSING RUN ON OPERATIONS BY RETAIL DEPOSITORS, SEPTEMBER 16, 2008
1898	8233	MINUTES - MEETING OF THE GOVERNMENT REPAYMENT COMMITTEE OF THE BOARD OF DIRECTORS OF AIG INC, SEPTEMBER 29, 2010 7AM [REDACTED]
1901	8172	EMAIL FROM JON D GREEN TO WILLIAM B ENGLISH RE: AIG CALL, EMAIL DETAILS TRISH'S NOTES ON CALL, SEPTEMBER 12, 2008

1924	8180	AIG'S OPEN/CLOSE/HIGH/LOW STOCK PRICE FROM 9/15/08 - 9/24/08 AND FROM 6/29/09
2701	8241	Dr. Saunders Demonstrative Slide
2702	8241	Dr. Saunders Demonstrative Slide
2703	8241	Dr. Saunders Demonstrative Slide
2704	8241	Dr. Saunders Demonstrative Slide
2705	8241	Dr. Saunders Demonstrative Slide
2706	8241	Dr. Saunders Demonstrative Slide
2707	8241	Dr. Saunders Demonstrative Slide
2708	8241	Dr. Saunders Demonstrative Slide
2709	8241	Dr. Saunders Demonstrative Slide
2710	8241	Dr. Saunders Demonstrative Slide
2711	8241	Dr. Saunders Demonstrative Slide
2712	8241	Dr. Saunders Demonstrative Slide
2713	8241	Dr. Saunders Demonstrative Slide
2714	8241	Dr. Saunders Demonstrative Slide
2715	8241	Dr. Saunders Demonstrative Slide
2716	8241	Dr. Saunders Demonstrative Slide
2717	8241	Dr. Saunders Demonstrative Slide
2718	8241	Dr. Saunders Demonstrative Slide
2719	8241	Dr. Saunders Demonstrative Slide
2720	8241	Dr. Saunders Demonstrative Slide
2721	8241	Dr. Saunders Demonstrative Slide
2722	8241	Dr. Saunders Demonstrative Slide
2723	8241	Dr. Saunders Demonstrative Slide

2724	8241	Dr. Saunders Demonstrative Slide
2725	8241	Dr. Saunders Demonstrative Slide
2726	8241	Dr. Saunders Demonstrative Slide
2727	8241	Dr. Saunders Demonstrative Slide
2728	8241	Dr. Saunders Demonstrative Slide
2729	8241	Dr. Saunders Demonstrative Slide
2730	8241	Dr. Saunders Demonstrative Slide
2731	8241	Dr. Saunders Demonstrative Slide
2732	8241	Dr. Saunders Demonstrative Slide
2733	8241	Dr. Saunders Demonstrative Slide
2734	8241	Dr. Saunders Demonstrative Slide
2735	8241	Dr. Saunders Demonstrative Slide
2736	8241	Dr. Saunders Demonstrative Slide
2737	8241	Dr. Saunders Demonstrative Slide
2738	8241	Dr. Saunders Demonstrative Slide
2739	8241	Dr. Saunders Demonstrative Slide
2740	8241	Dr. Saunders Demonstrative Slide
2741	8241	Dr. Saunders Demonstrative Slide
2742	8241	Dr. Saunders Demonstrative Slide
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2744	8241	Dr. Saunders Demonstrative Slide
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2764	8241	Dr. Saunders Demonstrative Slide
2765	8241	Dr. Saunders Demonstrative Slide
2766	8241	Dr. Saunders Demonstrative Slide
2768	8241	Dr. Saunders Demonstrative Slide