C O N F I D E N T I A L

FINANCIAL CRISIS INQUIRY COMMISSION

Interview of ILYA KOLCHINSKY

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BRUCE McWILLIAMS (via phone)

BY MR. BONDI:

Q Good morning, Mr. Kolchinsky. My name is Brad Bondi. I am with the Financial Crisis Inquiry Commission in Washington. We are an independent commission formed by Congress to investigate the causes of the financial crisis and to do a report for the American people. I am joined today by my colleagues, Ryan Bubb, Tom Borgers, Bruce McWilliams by phone, and we have a court reporter today.

We wanted to ask you a few questions concerning your tenure at Moody's Corporation.

A Sure.

Q For the record, could you just state your full name and spell it, please?

A My full name is Ilya Eric Kolchinsky. The first name is I-L-Y-A, middle name is E-R-I-C, last name is K-O-L-C-H-I-N-S-K-Y.

Q And Mr. Kolchinsky, if you could briefly describe your educational background?

A I have a Bachelor's of Science in

aerospace engineering from the University of Southern California. I have a J.D. from New York University School of Law. I have an M.S. in statistics from the New York University Stern School of Business.

Q And did you receive your J.D. before your statistical degree?

A It was at the same time. I was an engineer, I went to law school, just because I guess I didn't know what else to do. So as I progressed through law school, I actually loved law school; I know a lot of people don't say that. I loved law school. I realized I didn't want to be a lawyer, so I arranged a joint degree with the business school so I can get into finance.

I didn't want to do the full MBA, but I thought if I got an M.S. in stats from a business school, that would give me enough of a push. I spent three months as an attorney with Willkie Farr Gallagher and processed a lot of FedExes at the time, prior to PDFs.

You are an attorney and you are

an attorney also?

Q Yes. Mr. Bubb and I are both attorneys. Mr. Borgers and Mr. McWilliams are not attorneys. Mr. Bubb, though, if I am permitted to say, is actually going to be teaching in the fall at your alma mater.

A Great place. I had a great time. It was a great experience. I don't know if it has changed since then, but I had a fantastic experience.

Q Mr. Kolchinsky, could you briefly describe your employment history after leaving NYU?

A Sure. I worked at Willkie Farr Gallagher about three months, and then I went to Goldman Sachs where I spent about a year and a half in the CMBS group, commercial mortgage-backed securities.

I went over to Merrill into their new-fangled, they called them CBO and CLO, collateralized bond obligations and collateralized loan obligations. Now they are all called CDOs, which are collateralized debt obligations, but it was the early part of the market.

I stayed at Merrill for about six months involuntarily. It was after Long Term Capital, they had a large layoff. I was laid off. I thought I would try to give something more stable a try. I went to MBIA, which is a large bond insurer, or was a large, still a bond insurer.

After MBIA I went to Moody's. I stayed there for four years, decided to give banking another try. I went to Lehman for a year. I went to -- Lehman was a great place, but at that point I already had two kids, living in the suburbs, and the lifestyle didn't really work, so I went back to Moody's where I stayed in the rating agency. So this was, I went back to Moody's in '05, May '05.

I stayed at the rating agency until I guess officially November '07, at which point I was asked to leave. I was asked to leave earlier, in late October, but I officially was transferred out in November.

Q Now, you mentioned initially

spending four years at Moody's before you went to Lehman. When were those four years?

A That was from 2000 till 2004.

Q And what group were you in from 2000 to 2004?

A CDO derivatives.

Q Who did you report to from 2000 to 2004 in the CDO derivatives group at Moody's?

A I think for the vast majority of time I reported to Gus Harris. I think there might have been a switch at the end. There were several managing directors in the group and I occasionally switched between which managing director, but I think for the vast bulk of the time I reported to Gus Harris, H-A-R-R-I-S.

Q And what was your title from 2000 to 2004?

A I started as a vice president senior analyst, and I was promoted to vice president senior credit officer. I left as vice president senior credit officer.

Q And when was your last day, if

you remember, in 2004 before you left?

A Sometime in May. I don't remember.

Q May of 2004?

A Yes.

Q And when you returned to Moody's in 2005 --

A It was also -- it ended up to be like nearly a year almost to the day, but I don't recall off the top of my head.

Q And what was your title when you returned to Moody's in May of 2005?

A It was, I returned as vice president senior credit officer. I was then promoted to senior vice president, and then finally promoted to managing director.

Q And when you returned to Moody's in 2005, to whom did you report?

A I think I had two lines of reporting. I think I had one line to Gus Harris on a, I believe, for the -- I ran a small group of folks who worked on some of the software, modeling software that we were building in-house, I think it was called

CDOedge, one word. And on the analytical side I believe I reported to Gary Witt.

Q And Mr. Kolchinsky, if you wouldn't mind, spell names as we go; just that way we have a clean indication of the spelling.

A Sure.

Q Clear indication of the spelling.

Let's first take your first period with Moody's from 2000 to 2004.

A Uh-huh.

Q What model was being used by Moody's to rate CDOs?

A Well, when you say model, there is a lot of models. Let me see if I can sort of distinctly box those around.

First you needed to have, in any approach you needed a credit model. Now, do you want to know CDOs in general or the whole spectrum of things, because there is sort of twists and turns.

So if you think about sort of an evaluation or a ratings process for structured finance, you have a credit model to start with which outputs to some sort of a waterfall model, and then from that waterfall model you have some results at the specific tranche level which you analyze. So if it is a valuation you assign a number to it; if it is a rating you assign a rating to it, so this is tranche specific results.

For the credit model, the theory didn't change much in the sense that the credit depended on the underlying ratings.

What the other model I think a lot of folks and I think you are getting to, so that gives you the mean of the distribution, so now you need to figure out what the shape is, and we used the diversity score. It was calculated differently for, as I recall, for corporate credit, and that diversity score I believe is almost unchanged today. And we used a different, I believe a different diversity score at that time for CDOs backed by other structured assets, and that was called a two moment method. I don't remember exactly when it was put in place, but that was the large

portion of the time that I spent there.

That basic two moment method was used in correlation to that two moment method. It changed over time, so there was a lot of, it was an open model in the sense it was an Excel spreadsheet, so you can change the correlations.

So there is a lot of tweaks to this model.

Q Now, specifically speaking about --

A I am sorry. There is also an emerging market diversity score model, but I didn't work on emerging markets.

Q Specifically speaking about the models used for CDOs where the underlying collateral was primarily RMBS, or residential mortgage-backed securities, from 2000 to 2004, what model was being utilized by Moody's to rate CDOs where the underlying collateral was residential mortgage-backed securities?

A Two things. During that period the vast majority of the deals that were backed by structured credit only had small

allocations to RMBS. They were called resect deals because they were almost a kitchen sink approach. So they included aircraft, they included mutual fund fees, what else? Manufactured housing, all these things that ended up blowing up in the first credit cycle in the early 2000s.

So the advent of the truly subprime RMBS backed ABS CDO didn't come until late in that period, somewhere in '03, '04, '05. The earlier deals were primarily kitchen sink type, throw in a little bit of everything.

Part of at least the Wall Street marketing of these deals is that if you looked at collateral in the early cycle deals, the one asset that performed relatively well compared to manufactured housing, compared to mutual fund fees, et cetera, was the residential bonds. So, and I think lot of this was salesmanship, but what bankers said, well, who is going to walk away from a house? Americans never walk away from their homes.

So little by little they became less sort of kitchen sink but more residential backed transactions.

Q Now, in 2003 and 2004 when these CDOs with RMBS as the collateral started to gain in popularity in the marketplace, were there any conversations within Moody's that you are aware of concerning how to model those types of CDOs? Were there any such conversations?

A Yes, I believe there were, but a lot of -- the mentality we had, rightly or wrongly, is the credit, the mean, the credit, comes from another part of the rating agency. We are not going to question that. What we try to focus on are the dynamics within the CDO itself. It is a tradable pool, so we looked at how the trading dynamics work.

For example, I believe we started -- I don't know when it was started, I believe it was during my first go-around -- discount purchase rules. So the first generation of CBOs we saw in a credit cycle, that sort of early part of the century credit cycle, 2000, 2001. Those deals, if you bought any bond, as long as it wasn't defaulted, you got full par credit. So if, for example, if a bond was set to pay back $200, you got $200 worth, unless it was defaulted.

So what we saw as managers buying some of these bonds at very highly discounted prices, in order to build up par in the deal, artificially, of course, if they bought something at 50, 60 cents on the dollar, the market was telling you something and they would default.

So we implemented a discount purchase rule, and that essentially said if you buy something below 75, the only par credit you get in the transaction is to your purchase price. So if you buy at 50, you only get 50.

MR. BUBB: When was that implemented?

THE WITNESS: I don't recall exactly. I think it was somewhere between 2000, 2004. There may be a

research piece on it somewhere.

MR. BUBB: It is called a discount purchase rule?

THE WITNESS: When I came back I actually wrote, I don't know if this is -- I was a co-author on another research piece on the discount purchase rule.

So that I believe also during the first, that first time we implemented, again these transactions had overcollateralization tests, so in the waterfall you have an interest waterfall and a principal waterfall. This is a periodic waterfall.

Interest will pay taxes, fees at the top, pay the top tranche interest, pay the next tranche interest, and then there would be the overcollateralization test, and that is assets over liabilities. So if your assets decline below a certain level, you would trap that interest to the waterfall that would otherwise

fall lower and use that interest to pay down the notes.

One thing we did, I believe it was at that time, implemented haircuts for structured securities. The idea there was that technically, you know, if you think about the way that the overcollateral test works, it is assets over liabilities. What is the par value of an asset?

Well, again, unless it is a discount purchase you have got full par credit, but what we said is, well, you know what -- unless the asset was a defaulted asset. Structured assets don't really technically default. They default at maturity, so they can have all kinds of stress, credit stress until then.

So in order to sort of keep the same dynamic, there were haircuts. So if something was rated BA, you got one type of haircut; single B, it was another stronger haircut; C double A

was even a higher haircut, NOC test.

That whole idea, sort of early signals of credit deterioration, and you can reroute that interest and principal, the principal waterfall to pay down the note. So those are, you know, these are mostly here in the waterfall, but those are the kinds of things we really talked about a lot.

I know there is probably some conversations on the diversity score correlations. I didn't have a lot of input on that. People sort of picked their area. I just was not involved in the correlations, not much.

BY MR. BONDI:

Q When RMBS CDOs -- and I will use that term throughout the interview --

A Sure.

Q -- to mean CDOs that have collateral that is primarily consisting of residential mortgage-backed securities.

A Yes.

Q When RMBS CDOs were gaining in

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popularity, are you aware of any conversations within Moody's concerning the effect on market share if Moody's utilized a particular model or approach to rating RMBS CDOs?

A No, I don't recall. I think if they did occur, I think a critical part of it was actually when I was at Lehman in '04, '05, so I do not recall.

Q We have heard of a model called the binomial expansion technique?

A This was the original diversity score.

Q Or the BET model?

A Yes.

Q Just for ease of saying, we will just refer to the binomial expansion technique as the BET model.

A Sure, or you can call it the diversity score as well. It is equivalent.

Q The BET model, was that something that was in existence when you arrived at Moody's in 2000?

A Yes.

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Q And was that used to rate RMBS CDOs in that time period from 2000 to 2004 before you left to go to Lehman Brothers?

A Well, there is two parts to the BET.

The corporate BET has been around for a while, and it was a very simple, almost intuitive approach. What the -- the way the BET worked is that you assume a binomial distribution, which is a discrete problem and distribution. The key to that was figuring out what the diversity score, how many diversity independent bonds.

So binomial distribution requires IID, independent identically distributed rating variables. The whole idea is you take this pool of correlated assets and you distill from that how many truly independent assets there are, uncorrelated, and from that, having those assets, using the average default probability from the underlying ratings, you can create a probable distribution of all events in the portfolio.

The question is how do you

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calculate those diversity bonds, how many truly IID bond there are.

MR. BONDI: Can we take one quick break?

(Brief break.)

THE WITNESS: So that is the binomial expansion technique. But the way you arrive at the diversity bond, the IID bonds, for corporate, I remember that being around forever, I remember before I even joined Moody's.

For deals that are backed by RMBS or backed by other structured assets, for the vast majority of my first tenure there we used what is called a two moment diversity score method. I don't remember if we used it when I first started. I don't think I did a lot of it when I first started, but during most of my tenure, that is what was used.

Now, that too was an Excel spreadsheet. It had a matrix of correlations that were displayed. It

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was tweaked a number of times. Part of the problem is that folks didn't know which model is the latest model. One deal would use one model and the next deal would use another model.

So in terms of -- there is two aspects of it. There is the distribution itself, the probability distribution, and there is the correlations. So in '04, up until '04 for the distribution we still used the binomial distribution, and the correlations came from the two moment model which was updated regularly and chaotically. And I don't remember if it was that way from the day I started, but for the vast bulk of the time there, the two moment method was used to set the correlations.

BY MR. BONDI:

Q Who was responsible for updating the two moment correlation?

A It kind of went back and forth. I think -- I don't remember. I think by the end of it it was charged to David Ham, but I don't know if he officially -- the group in some ways when I started was chaotic and in some ways resembled an academic department. There was boxes, books, there wasn't a lot of structure in the unit. It was a small group, not that many deals. So it was chaotic.

So a lot of times people's responsibilities just came from, you know what? You updated last, and then everybody starts coming to you and then it becomes your responsibility and you update. I think David Ham was the person responsible, but to be honest with you, I am not sure.

MR. BUBB: What was the updater supposed to be doing? Was it based on historical data or --

THE WITNESS: I think so, but I am not sure. I was not involved in the correlation setting. My interest, to be honest with you, was sort of in the waterfall model side of things, so that is where my expertise came and

that is where I was sort of the specialist. But on the correlations, I --

BY MR. BONDI:

Q And if you could, in this time period before you left Moody's to go to Lehman Brothers, in the 2003 or 2004 time period, let's take 2004.

If an RMBS CDO was to be rated and the collateral, much of the collateral came from RMBS from let's say Countrywide, let's also say for this example that Citigroup was the issuer. Can you take us through in 2004, early 2004, how you would go about rating that CDO?

A Sure.

Q What would the models be, what would you look to, what that process was involved? If you could just take it through, start to finish of a rating, a typical RMBS CDO rating in early 2004.

A We rated most -- because they are tradable pools, we didn't really look at the collateral as much as probably we should

have, but the idea was because there is an active manager, the manager can buy and sell, looking at any particular portfolio is probably not as useful as it could be.

Q Now, you mentioned an active manager. You mean an active manager on the CDO deal?

A Yes. There is usually a collateral manager, somebody who theoretically has experience in the area, who is in charge of selecting the portfolio and buying and selling the collateral.

So we would receive -- again this was a little bit more chaotic -- at that point we would receive the indenture for the deal. We would rate off the indenture only. In some cases we would receive the waterfall model. At that point there was no standard waterfall model, and I had my own personal model which I built myself, an Excel spreadsheet.

A lot of people audited the bankers' models, and there is one gentleman, John Parks, started at that time

standardizing his own model, which then became the standard model for everybody. But I used my own that I developed model.

So the idea was you would take the data in from what the covenants were going to be for the transaction in terms of weighted average life, weighted average rating factor, also known as WARF. The WARF is a numerical representation of a rating. It goes from one to 10,000. It is supposed to be the idealized ten-year default probability, and it just allows you to communicate ratings which are alphanumeric and purely numeric. The weighted average, you can manipulate them.

Weighted average life, weighted average rating factor, weighted average recovery rate, all these factors, weighted average coupon, weighted average spread, the proportion between fixed and floating collateral, things like that. We would look at the indenture, the waterfall with priority of payments. We talked about how to allocate the money on a periodic basis.

That would be built into a cash flow model, waterfall model, and you would try to ensure at that point -- we didn't do much with the actual diversity score method because again partly it was like a blindness one way or another. Because it is a tradable pool, we just assumed the bankers would calculate the diversity score, the manager would calculate it correctly. It was, the model was available for free, the two moment model, to any market participant. They had to sign some sort of a confidentiality form, but it was available to anybody who wanted it.

You know, we would make comments on the indenture, we would make comments on, if we did not -- the way we worked, I know this is different from some other areas at Moody's, we just gave a pass or fail on the rating. So the bankers would come to us with a capital structure with all of the covenant levels and we would say, well, I agree that, given this setup, you get to the ratings, or I don't agree. Obviously if you

don't agree you try to figure out what is going on, but we wouldn't provide back subordination levels like they did in RMBS, CDS. It was a very open model. It was a yea or nay essentially.

A lot of this stuff actually, whether it was working around comments on the indenture, make sure they conformed to the model and assumptions that we used, so the model in the waterfall conformed to the actual legal documents.

Occasionally you wouldn't, you would say nay on the quantitative results, in which case there was usually -- there was always a quantitative analyst and a legal analyst on each transaction, so the quantitative analyst would just basically talk with the banker to make sure how the model is off or not, who is right or wrong.

Most of these cases they were all Excel spreadsheets, and being Excel spreadsheets there is a high tendency to somebody accidentally deleting a cell when doing it or hard wiring a cell. So a lot of

times it was either the rating analyst or the banker just was sloppy. If that was the case, if it was the banker's fault, they would come back with a structure that would pass, and if it was the analyst they would adjust their model and it was okay.

So that is sort of the day-to-day of rating a transaction.

Q Now, Mr. Kolchinsky, were you the quantitative analyst?

A I was the quantitative analyst, yes.

Q And then you had a counterpart who was a legal analyst?

A Yes.

Q And who was the legal analyst who was your counterpart in the 2003, 2004 time frame? Would it have varied?

A It would vary. There were fewer legal analysts than quantitative analysts, so the quantitative analysts did the bulk of the work.

The legal analysts, they would also check the opinions, make sure the true

sale opinion was there, all those kinds of legal niceties that we on the quantitative side didn't bother ourselves with. But the bulk of the work on any deal would be done by the quantitative analyst. The legal analyst would be there for support.

A lot of times I liked that kind of a staffing structure because there is two pairs of eyeballs at every deal. If somebody misses something, somebody else would get it. So even if two quantitative analysts, it was nicer to have two pairs of eyeballs.

Q Now, let's if we may just put some concrete names behind this hypothetical. Citigroup is the issuer, underwriter.

A Yes.

Q Say Pimco is the manager of the deal.

A Okay.

Q And the collateral, most of the collateral is RMBS from Countrywide.

A Okay.

Q How would the CDO deal, in early 2004, this particular deal that I have described, how would it first enter the door? Would it be someone picked up the phone from Citigroup or someone picked up the phone from the manager and called Moody's?

A For the most part it would be the banker, the banker would call Moody's.

Q Somebody from Citigroup --

A Yes.

Q -- would call on Moody's?

A Could call a managing director who will then staff the transaction. Then you had to find out, okay, you are working on this deal, here's the contact at the banker, you know, start talking.

Theoretically it could have been the collateral manager, it would have had to have been somebody who has a lot of weight, but I don't off the top of my head recall any instances where the collateral manager would have picked up the phone. It was primarily the bankers.

Q And when the banker would pick up the phone and call Moody's managing director, at that point would the banker present the structure to Moody's? When was the structure actually presented?

A That was -- it depended. Before we could do any work we usually said we need at least some copy of the indenture, and we needed a -- depending on, like I said, at that point it was chaotic. I had my model. People who had their own model said just send me the covenant you intend to use for the deal.

The indentures were usually the typical square brackets in the first couple of drafts. Then when you get the final indenture you get the first draft. So most of the covenants were just empty square brackets. So they would send you a spreadsheet with this is the covenant's weighted average, rating factor, et cetera, et cetera.

That is when it would start, but we definitely wanted at least an indenture

and those covenants to do anything.

MR. BORGERS: Mr. Kolchinsky, during this time, didn't the bankers actually tell you what was in the pipeline, that they have one, two, three deals coming in and alert Moody's that, hey, listen, we have three deals coming in, here it is, A, B and C?

THE WITNESS: Sometimes that occurred. That is probably more of a conversation that they would have had with the managing director. Sometimes, for example, I worked a lot of deals with Bear Stearns, and through just general conversation they would tell me what is going on.

The other change, practical change between my first -- well, let's say between cash deals and synthetic deals, credit default swaps, CDS-based deals, the cash deals by definition required some period of time to actually ramp up. So a banker, you

know, it would probably be six to nine months from the start of the deal to closing.

So six to nine months from the time that the banker approached the collateral manager with a proposal, the collateral manager agreed, they negotiated a warehouse agreement, they negotiated all kinds of agreements, and at that point the collateral manager would start ramping up the transaction, meaning he would either buy things in the secondary or more likely buy things in the primary for the warehouse, and the banker would monitor the warehouse.

They usually, when I was at Lehman we had veto power, so any kind of thing that the manager wanted to buy, the trader on the desk would say yea or nay because, although the manager usually took some risk in the warehouse, the bulk of the risk was taken by the banks, so the trader

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would say yea or nay.

But as that got to a critical mass point, maybe about 60 percent, then you would start, you know, as the banker, since I was in banking, you would approach a law firm to start working on the legal documents, you would approach, set up the accounts, you would approach the trustee, set up the trustee for the transaction.

Then probably maybe two months before you intended to close you would approach the rating agencies: Here's the deal that I have, here's the manager, here's the first draft of the indenture, and here's what I think I want the pool to be like. You as a banker, because most of the rating agencies, at least in the CDOs that were sort of open model, you were running the ratings at every point.

So when I was a banker, both at Merrill, we had these models, and each time a bond came in the warehouse, I

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would adjust the covenants to see where I had to be in order to hit a certain equity return or whatever, however we needed to market this deal, and I'd get back some information from the traders on the liabilities, credits, all that kind of information including the rating agencies.

So about two months before that, on the cash side, all this process took time, then you would approach the rating agencies, and at that point the deal was 60, 70 percent banked. You as the banker have been running models; like I said, it was an open source type of a thing for the most part. You would deliver here is the deal, here is the indenture.

And we would spend about two months, one month on the deal at the rating agency, commenting on the drafts of the indenture, commenting on the covenant and the quantitative information, and so would the trustee,

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so would the collateral manager. So bankers kind of coordinate all the information and you would get periodic drafts. First you would read the indenture, then just look at the black lines, so on and so forth. So that is the sort of the process.

What changed after credit default swaps. CDS, is that you could all of a sudden ramp up a deal in a week, the whole, here's the listing. So that really sped up the process to the point where we were sort of in late '06, '07, a lot of effort was sort of slow down the bankers.

BY MR. BONDI:

Q I definitely want to get to the synthetic deals, but I don't want to leave this thought at the moment in terms of what was going on in '04 --

A Sure.

Q -- before you left to go to Lehman, just the typical cash RMBS CDO.

A Yes.

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Q So, you described the process.

A Yes.

Q You have the indenture --

A Yes.

Q -- agreement with some black line, black lines.

A Yes.

Q You have looked at the deal, you have analyzed the deal.

When does the ratings committee begin to meet?

A At that point we try to meet, at some point that we felt that the -- if you are a good analyst and there is something controversial in the deal, you telegraph that to senior people ahead of time, and most analysts follow that method, so by the time you actually have the committee meeting there is not a lot of surprises. It is very perfunctory.

When I began, the group was small and it was very possible to actually -- you were encouraged to talk to other analysts, just to make sure everybody was doing the

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same thing, talk to -- the managing directors for the most part ran the committees. If there was something controversial, a good analyst would bring it up on somebody's radar immediately.

So by the time you had a committee, which would probably be a week or so, as I recall, before closing, there is not a lot of surprises. And a lot of them just described the transaction, you would describe what the issues were, how they were solved, and what their recommendation is for the rating.

Q In 2004, how did the ratings committees operate? What was the function of the ratings committee, who was on the ratings committee?

A Everything was very chaotic. I believe, this is a while back, it had to include at least one managing director and that is it. Sometimes it would be as few as two people. There usually had to be the quantitative analyst and the managing director, and it could be larger.

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Q So, going back to my example with the Citigroup RMBS CDO, Pimco as the manager, the underlying collateral was largely from Countrywide, you have gone back and forth on the indenture agreement, you have looked at the deal. And then is it your position then as a quantitative analyst to bring the deal to the ratings committee?

A Yes.

Q And then how would you bring the deal to the ratings committee?

A I would usually have some sort of a memo. And again, the early days were very chaotic. Memos ranged from two pages to very elaborate memos. That is something that they started working on, to getting more standardized rating memos. But I think at the end we were actually -- I will give you an example.

We were asked to write and would issue reports for every deal, these research papers. So what I actually did is, to save myself a lot of double work, I actually drafted the committee memo as a new issue

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report with some things on the back that were solely for the ratings committee, like the actual quantitative runs. But I would actually draft it as a new issue report. That way when I am done, just rip out the sort of internal things, PDF it, and boom, out it goes.

But there was no standard requirement on how you draft a committee memo.

Q 2004, though, this hypothetical CDO, you draft a memo to whom? To the managing director?

A To the committee members, whoever was going to be attending the committee.

I don't even know if I -- there is a committee memo in the, if you have the documents from the -- a later committee memo, but if you have the documents from the Senate permanent committee, there is actually a late vintage committee memo in there.

But that was post attempts at standardization, because it was fine when we

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were small and the deal flow was very low so you could, you literally, a good analyst would check with everyone all these points and just make sure that everything was set up. But as the group grew bigger and the deal flow got even bigger, there was just more need for standardization.

Q I am having trouble understanding what came first in the chronology here.

The ratings memorandum that you described, was it called a ratings memorandum?

A Yes, ratings memo.

Q The ratings memo, you indicated that that would be sent to the ratings committee?

A Yes.

Q So, can I assume, then, that the ratings committee was formed first?

A The ratings committee was at that point, as I recall, was ad hoc. So, I have a deal, it is sort of -- I only needed one managing director for the ratings committee, so I am ready to go to committee.

Q You meaning as the quantitative analyst?

A I set up a meeting with Outlook with that managing director. I try to invite other managing directors to the meeting, the legal analyst. If everyone accepts, I send out the memo to those people, but it was ad hoc. At some point it was even up to the analyst to play games of which managing director do I want on my committee. Some of them were more inquisitive and others were less inquisitive.

Q So, let me get this straight.

It is early 2004, you are the quantitative analyst, you have a deal that you want to have rated, and you need to get it rated by the ratings committee?

A Yes.

Q So you send out a calendar invite in Outlook --

A Yes.

Q -- to the persons that you went on the ratings committee?

A Yes. I believe that was the practical way we did it.

Q And depending on who accepted your Outlook invitation, that is who you knew you would put on the "to" line of the ratings memo?

A If I even had a "to" line. This was very chaotic in the beginning, so I would have sometimes drafted it as a, like I said, a new issue report.

Q In early 2004, in this time period, who was Brian Clarkson? What was his role?

A I don't remember exactly. At that time, to be honest with you, I was sort of kind of going in there, punching the clock. I don't remember who -- I mean obviously he was either -- I don't remember at that point if he was already in charge of the derivatives group.

I dealt with him at some point. I don't remember at what point I dealt with him. There was a whole controversy about notching, so Moody's hired NERA, National

Economic Research Association, to do a research report. I contributed some stuff, and Brian was happy with it, gave me a sweatshirt, something like that, and I think that was before, so I think he was pretty high up.

I don't remember what his title was, to be honest with you. He wasn't -- I don't think he was the head of all structured. I think he was the head of maybe CMBS and derivatives. I don't recall exactly.

Q In early 2004, going back to our hypothetical deal here, how important was it for you as the quantitative analyst to obtain the sign-off from the rating committee for the rating that you are proposing in your ratings memoranda?

A It was critical. The rating didn't go out unless the committee agreed officially. The committee had to have agreed to the rating.

A lot of times it was a rubber stamp, or if you had a good analyst you

wouldn't get a lot of questions, so it wasn't -- but it was not, it was impossible to send out a ratings letter without having the committee okay it, even if that committee was two people.

Q Now, in early 2004 you described the process as being ad hoc.

A Yes.

Q But what generally, in early 2004 --

A They were starting to standardize things, but it didn't really get to that point.

Q In early 2004, what would you put in a ratings memorandum that would go to this ratings committee?

A The capital structure, the covenant, descriptions of the waterfall, descriptions of OC tests, descriptions -- overcollateralization tests, descriptions of any sort of a swap or a cap or four in transaction, a description of the collateral manager, what they have worked on before, who the banker is, and the model results.

I would also put in if there were

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some issues that were particular to this transaction and how they were resolved.

Q Would you also include any reference to future deals from that banker?

A No, I don't recall anything like that.

Q And in early 2004, as a quantitative analyst, how would you have been compensated?

A Well, you had your base pay, you had a target bonus, and you had a, some equity participation, equity bonus, a cash bonus, some sort of restricted stock options bonus.

Q And how was your cash bonus calculated?

A I think I know what you are trying to ask, was it based on the number of deals that you did. The answer is no, for good or for bad, in terms of there were analysts who only worked one or two deals a year, and either because there was a lot of sort of I guess favoritism in the group, either because someone is favored or because

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they were doing a lot of research, they might get a good bonus. On the other side, there could be an analyst who worked on a lot of deals who may not get a good bonus.

So there was no, the connection if everybody saw it sort of to the equity portion and the stock price, how much equity do I have, you know, where the stock price is. So people had options, people had restricted stock.

But the cash bonus in the bonus pool that was funded depended on how well the company did in terms of revenues.

Q How well the committee did in terms of --

A No. The bonus pool was a function of how well the company did with respect to revenues.

Q So the more money you made, the more everyone benefitted --

A Yes.

Q -- financially.

A Yes. And I believe there is a chart, and there was always a lot of leeway,

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but there was a chart in terms of how well the company did versus budget and people's ranking.

People would be ranked five, four, three or two. Almost no one was five unless they were junior. And for each point, it is a matrix in terms of what is your rating and how much over budget the company went, that is how the bonus pool was funded, I believe. I believe that was the case up until I left.

Q Focusing still on this early 2004 time frame, you described earlier what might be called forum shopping with picking certain ratings committee members.

A Yes.

Q Do you know that to have taken place in this time period of 2004 or earlier on RMBS CDOs?

A Forum shopping between committee members?

Q Yes.

A Yeah. I don't have concrete examples, but I remember people talking

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about, you know, don't hire this MD, he is going to ask too many question, go with this other MD, it is much easier. The analyst did that. But from the analyst's perspective, I always assumed it was more of a sign of laziness than anything else.

Q In early 2004, who were the more difficult managing directors that may have composed ratings committees?

A I don't remember -- the two most difficult ones were Jerry Gluck, and the other -- he left under mysterious circumstances. His name is Isaac Efrat; I don't know if you have spoken to him.

Q Isaac, and the last name?

A Efrat, E-F-R-A-T. He departed Moody's under mysterious circumstances.

Q Do you know where Mr. Efrat is today?

A He is at Aladdin, which is a hedge fund. It is not spelled in the standard way because it is named after the owner, who was born in Nigeria and then actually grew up in Japan. So it is very

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interesting, he is a very interesting man, but it is not spelled in the normal Aladdin. I forget how it is spelled, but the number of Ds and Ls is not standard:

He had the nickname of Dr. No: He was a Ph.D., so hence the doctor. And --

Q When did Dr. Efrat leave Moody's?

A I don't recall. It was I believe before I left Moody's.

Q Did you hear any rumors about why he left Moody's?

A Well, the rumors were swirling that he left because he said no too many times. He wasn't, he didn't leave himself, he was asked. But that was just rumor, pure, pure hearsay.

I've talked to him since. He hasn't talked about why. He doesn't want to discuss it. It is purely rumor.

Q In 2004, the early 2004 time period, who were the easy managing directors who didn't ask a lot of questions about deals?

A The other two was Gus Harris and Bill May, M-A-Y.

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That doesn't ask a lot of questions? Gus is my mentor. A lot of times he worked on a trust basis, so he focused on people he trusted to carry out the deal, that is fine. So he is my mentor, but, you know, if he trusted you, he just didn't ask a lot of questions.

Q How many times did a ratings committee, in your first tenure at Moody's, how many times did a ratings committee say no to an RMBS CDO?

A No -- well, to be honest with you, it wouldn't happen at the committee to say no. If we were to say no, it would have occurred way before that point.

In two months of time, if something just didn't work out right, again, from sort of managing expectations on the banker's side, you are told as an analyst if you have a problem, don't sit on it, communicate it to everybody. Don't sort of raise it to a level where deals are at the closing and you say, look, I can't get to this rating. If there was a problem with

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the deal that was there the first time, you'd better have communicated to the banker. It shouldn't happen at the committee level. So that is why they talk about if there is a problem, you talk to people, you talk about it.

I don't remember how many times we said no to an RMBS backed deal. I do remember in the early days we said no to quite a few. When I first started I can imagine it happening -- this was 2000, I was asked to look at a transaction backed by all telecommunications bonds. Remember, this is after the tech bust, so everybody had too many telecommunications bonds. And I looked at it, I said we can't, it doesn't work, it just doesn't work at all, okay, and that was that. We said no to that deal. So that was not a problem at all.

Q Going back to the hypothetical example in early 2004, Citigroup, the bankers from Citigroup bringing the RMBS CDO backed deal, would they have said to you going in what they expected the ratings

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would be for each of the tranches?

A Yes, absolutely, because they had to, they have been running the models, so all we would do is say yea or nay to whatever structure they proposed.

But they would be running the models, so they would say here's my capital structure, hypothetically a hundred million dollars of triple A, I have 25 of double A, ten of single A, five B double A and 25 of equity, and it is backed by some amount of collateral that is going to be used. This is what we would like you to give feedback on.

Q How much pressure did you receive in your first tenure at Moody's from the bankers to agree to certain ratings on CDOs backed by RMBS?

A Any CDOs, I don't remember specifically. A lot.

Q What kind of pressure would you receive?

A This is crazy, why are you penalizing us, we just saw a different deal? It was all sorts of things; okay, we used

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this assumption in a previous deal, your model is wrong, anything and everything if the numbers didn't come out. But, yeah, anything and everything.

I don't recall at the sort of junior level the pressure level to take this deal elsewhere. Occasionally they might say, well, S&P doesn't look at it this way, Fitch doesn't look at it this way, but that is about as bad as it got.

Q As a quantitative analyst, would bankers threaten to call your supervisor?

A Of course. I would tell them, you don't like this? Call my supervisor. It was expected. It was expected. A good supervisor would defend their analyst, obviously, but that was pretty much expected.

Q In 2004, how important was market share to Moody's in ABS CDO route?

A I don't think I viewed it -- like I said, I wasn't in management, I wasn't, I was just doing my work.

Q Did anyone ever express to you in

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2004, though, we need to grow market share or we need to maintain market share in CDOs backed by RMBS?

A I don't think it was directly.

I think Brian, I don't remember if it was '04, but he always loved to put up his slides of things we used to rate. He loved these slides. He had slides of starting in 1990 these are the only kind of structured finance deals we rated, and now it is -- there was maybe six, and now it is three columns wide, all these things we rate. So there was an attitude, there was a push for people to have a can-do attitude.

Some of it was, frankly, some of it was frankly defensible. For example, there were some analysts who were just rude to people who called. I never believed in that way of doing business. I actually felt that I had -- and I had my share of fights with bankers and screams who were not my friends, but I always felt if you know people better, you have a better leg to stand on to tell them no, this just doesn't

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work. If they know you better, then they can't just completely lie to your face and say no, this should work, so they were more reasonable. So that was some part of it, but I think some of it was also purposely interpreted as just do the deal, get the deal done.

What I am trying to say is it wasn't all bad. Having good relationships with people you deal with is just good anywhere. And to me, I felt it always gave me more of a leg to stand on when I wanted to say no, this just doesn't work. People knew me. But there was a focus, I guess a can-do attitude.

Q Now, you stated earlier that you left for a time period, for almost a year to go to Lehman?

A Yes.

Q Were you rating deals for Lehman prior to joining Lehman?

A I think I did one or two deals.

Q And did you join the same group at Lehman for which you were rating their

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products?

A Yes.

Q Was that unusual, for someone from Moody's to leave to go become a banker?

A Not excessively unusual, no.

Q Were others at the time doing it as well?

A Others were, yes.

Q Who else do you recall leaving Moody's to go become a banker for deals that they used to rate?

A I would imagine quite a few folks. I don't remember, I don't know what the -- I actually have a different take on that.

I don't think there was a -- look, as a banker, if you had a rating agency analyst who was, for lack of a better word, malleable, you don't want that person as a banker. A banker's job is to push and push and push. From a banking perspective, I want somebody who has a backbone, and especially I think about, as a banker I have a rating agency that is malleable, the last

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thing I want is to move from a position that they are in. They are not going to be useful to me as a banker because they don't have the backbone to push all the other parties and shove this stuff down the other parties, and yet they are providing a great service to the rating agency. That is the last person I want to join my shop.

So that is my personal take on it. The people who left are the people who, you know, just think about the banker mentality, you know. It is very sort of type A. That is the kind of person who left, who gave a lot of back and forth to the bankers where they earned their respect and, you know, there was no reason to keep them at the rating agency. They wouldn't give you what you want. If they have that kind of skills, bring them on as a banker.

So I have a different take on that, and I know that has been, I know that has been circulated. I have a very different take on it.

Q Let me ask you, though, you've

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described people with, your words, with backbones that would go become bankers.

Do you believe, though, the prospect of becoming a banker may have influenced the ratings of individuals at Moody's who perhaps, using your term, did not have the backbone?

A It may have, but I don't know of any instances. Could it theoretically have crossed somebody's mind? Yes.

Q Would bankers use the prospect of potential employment to entice or influence employees at Moody's?

A Not that I am aware of, no.

Q So, you left to join Lehman.

A Uh-huh.

Q Just briefly, what did you do at Lehman?

A CDO structuring, the banking side of what I did at Moody's.

Q And why did you leave Lehman?

A Lifestyle.

Q And you mentioned earlier that you rejoined Moody's in May of 2005.

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A Yes.

Q Who was your boss when you rejoined Moody's in May 2005?

A I believe it was Gary Witt.

Q And how had Moody's changed in the year that you had been gone?

A It had become more standardized. They were rolling out sort of a secondary tier of management team leaders. Before it was managing directors and the rest of us, and they were rolling out a team leader concept to deal with all the deals, all the transactions in the market.

I think we had to be more market share focused. I can't really, to be honest with you, say specifically. I think it was more a slow buildup to that point on market share. I had heard from folks like Gary about these market share e-mails, but I didn't really, it wouldn't really trickle down to the analyst level. It was really at the managing director level.

You got those e-mails, you got inquiries, why wasn't this deal rated, why

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wasn't this deal rated. But I don't think it was that -- there was again a can-do attitude, there was more standardization, but I don't think at that point I felt that pressure directly on market share.

Q Now, eventually you described being promoted?

A Yes.

Q What was your first promotion upon returning to Moody's?

A Was to senior vice president.

Q And when was that?

A I believe, although I am not certain, it was in the summer of '06, but I'm not a hundred percent sure.

Q How did your duties and responsibilities change when you became a senior vice president in the summer of 2006?

A They didn't much, because even up to that point I had already given up -- to be honest with you, even from the beginning I started, walked into the team leader concept. I only rated one or two deals upon my return as an analyst, and then slowly but

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surely I started taking on the team leader.

And the idea behind the team leader, you had this sort of information glut around the managing directors. On the analytical side you have sort of a middle layer. So now, instead of just assigning, when you staff the committee, just assigning a quantitative analyst and a legal analyst, you also would have a committee chair role, and the role of that person was to make sure that they were, on the same type of deals, just make sure the deals were consistent across the board. There was a methodological consistency across all deals.

If an analyst had a question, instead of going to these managing directors, they would go to the team leader. The whole idea was that their communication was to happen at a team leader level and then come down to the analysts.

And when you set up a committee, I think by that time there was a, you started having more formal policies on who was supposed to be on each committee, so how

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many people, who gave what, et cetera, et cetera. So you were theoretically supposed to invite not just the managing director but all the committee, the team leaders for that product area as well, again so that there is consistency across the board.

Q Let's take a hypothetical deal again, the summer of 2006.

A Okay.

Q Bear Stearns, CDO backed by RMBS, and the banker at Bear Stearns comes to Moody's to rate the deal.

A Uh-huh.

Q How have things changed in the summer of 2006 as compared to in early 2004 when you were describing the rating process?

A Not really much. The only thing that changed is the time lines were starting to accelerate, because now you had more synthetic exposure. You had a more formal structure in terms of what was supposed to be in a committee memo, you had a more formal structure in terms of who was supposed to be on the committee.

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We were becoming -- the number of deals we did, our resourcing became strained. The number of deals we did in '04 compared to the number of deals we did in '06, there is a huge gulf, but our personnel did not go up accordingly. So I guess one change from when I started to let's say '06, '07, I started in something that looked like an academic department. We had time to talk. Actually at some points I had, we were at 99 Church Street -- I don't know if any of you are familiar with New York -- I had time to walk over twice a week to take French classes at the Alliance Francaise.

When I started I had all the time, no pressures; like I said, academic department. By the time I came back, definitely by '06 it became, my role as a team leader was crisis management. Each deal was a crisis. Bankers were pushing more aggressively, so that it became from a quiet little group to more of a machine. I can't say where that happened at what point, but that sort of started in a nice little

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quiet group where I can take three-hour lunches to essentially a rating machine.

Standardization was part of it. Everything was standardized. We had standard models which I helped to develop. There is benefits to the standardization. Some analysts, quantitative analysts weren't so quantitative. I really never believed that auditing a banker's model was very useful, so we had models on our own side. But then it became more of a factory, an assembly line.

MR. BUBB: Had the credit model changed since '04?

THE WITNESS: Yes, the credit model -- two ways. The correlations were now different, and instead of the binomial distribution we were using a correlated binomial distribution.

MR. BUBB: How had the correlations changed?

THE WITNESS: They were changed in a paper, I believe it came out in '05. They were based off of -- again,

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this is while I was at Lehman, so I can't give you the history of that. A paper came out, and Moody's revised assumptions for correlations, and a couple of things changed.

Prior to that, I think the two moment method had default correlations, and now we were using a model called CDO ROM. They are using asset correlations in the Merton sense.

The whole theory is, it is mostly with companies, but you have assets, the company is just assets that vary, and once they go below a certain level, that is when you have default, sort of a strike level. That was Merton's theory. But that was sort of the approach. So it went from default correlations technically to asset correlations.

Let me see if I have the -- those are the two. So there is two main changes. To me the correlation change was far more significant, as

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opposed to the binomial versus the correlated binomial.

BY MR. BONDI:

Q Why was the correlation change significant?

A I don't know. Why was it significant?

Q Yes.

A In some cases it went down a lot from before.

Q What is the significance of the correlation going down a lot?

A The significance is if you have a correlated distribution, you should have more risk on the test, more probability of higher events occurring, in the middle. So, as you are low in correlations, effectively you allow more of a triple A collateral, practically speaking.

Q So, in other words, the change in correlation that you saw from your first tenure at Moody's ending in 2004, compared to your second tenure at Moody's, was Moody's was using a correlation that allowed

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for higher ratings?

A Higher ratings at the top of the capital structure, because the way, the trick with the correlation is that the mean of the distribution does not change. It just changes the shape of the distribution. So it allowed more, I guess allowed more triple A.

Q And were the triple A ratings and the tranches contained in triple A, were they the ones that were driving the structure?

A Yes. If you look at, if you think of it from the cost of equity performance, which was the way that most bankers looked at it, what is the equity, the residual piece, what is the return, you would look at it in terms of what are my assets earning. So let's say that is LIBOR plus say 200 basis points, and then you look at your cost of funds.

The cost of funds, because the triple A piece is so large, are driven primarily by the triple A. Everything else

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is sort of a marginal contribution to the cost of funds. So let's say the cost of funds are LIBOR plus 150, so 50 basis points remaining for my equity, and then you multiply it by the leverage to get the current return. And that is how people thought about it.

MR. BUBB: If you had more triple A, what would that do to your cost of funds?

THE WITNESS: It would reduce your cost of funds.

MR. BUBB: Triple A was important to the bankers.

THE WITNESS: It was important to the bankers, yes.

BY MR. BONDI:

Q Having more triple A was important to the bankers?

A It was, yes. Also, triple A was easier to place.

Q Easier to sell, you mean?

A Sell.

Q Easier to sell triple A tranches

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of CDOs?

A Yes. At the time -- this is through the end of '05 -- there was pretty much one buyer of triple A RMBS CDO paper, and that was AIG. They were doing it through what was called a negative basis trade.

Q What is a negative basis trade?

A An account scenario, a CDO would originate a whole tranche of let's say super senior triple A. That triple A would be bought primarily by Yankee banks, and Yankee banks are foreign branches of banks operating in the U.S.

So if you look at who AIG owed money to besides Goldman Sachs, there was Soc Gen. So they would buy whole piece, they would buy the whole enchilada, and then they would enter into a credit default swap.

Q Let me interrupt for one moment just so I am clear. Soc Gen would buy the whole triple A tranche, you are saying?

A The whole super senior triple A tranche, absolutely.

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Q And then what would happen?

A Then they would go to a -- well, AIG, and later on there would become other parties for a credit default swap on that piece. So, theoretically they were taking funding risk while the Monoline took the credit risk. That is shorthand for financial guarantors and insurance companies such as MBI, Ambac and AIG. AIG wasn't in the Monoline, but they were in the same business.

And it was, I believe, I am not a huge expert, this was in their trading book at the banks, not the hold till maturity book, also known as the lending book, the normal book of business the banks do. This was in their trading book. And because it was considered hedged, they were able to present value all the money to day one.

So the profit basically, the way the economics worked, let's say this triple A paid LIBOR plus 40, and the credit default swap cost ten basis points, and this bank, usually a large foreign financial

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institution, could fund itself in the CP market at LIBOR minus ten.

If you look at the economics, it is 40 basis points minus ten, you basically have 40 basis points of annual profit and you multiply it essentially by, this is supposed to be outstanding for eight years, eight years, you know, that is your present value profit. So, in terms of accounting profits, it was very profitable for these banks.

That is how a lot of folks, Barclays was involved in it, pre-Lehman, Barclays, Soc Gen, a lot of folks did this trade. AIG was the biggest consumer, so they were basically the driving force behind all these deals.

Q How did the pressure change in the summer of 2006, that time frame, as compared to the earlier time frame of 2004. What additional types of pressure were you receiving from issuers?

A Well, as deals became -- well, at that time two things happened. The

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economics of these transactions started going down and down and down because of so many of them; as they were buying up all of the primary market RMBS, that was driving the spreads on the RMBS down. And again, the economics here, as the spreads on the asset side went down, that would lower the economics to the equity.

How do you offset that? Well, bankers needed to offset it, so they would force the cost of funds down by either trying to get more triple A, or by getting better triple A execution. So there is a couple of last minute entrants into the CDO, again primarily Yankee banks, whose whole pitch was we will also take the super senior, and they would do them at LIBOR plus 20. This is in late '06, some ridiculously low rates, so the economics would be better.

MR. BUBB: What do you mean by the term triple A execution?

THE WITNESS: The level at which it gets done, so it is the final spread to be paid on the triple As.

MR. BUBB: And that fell as they -- when you say better triple A execution, that means a lower spread on the triple A bonds because of the liabilities of the CDO.

THE WITNESS: Yes. So as the asset spreads went down, the bankers started to push down the liability spreads as well, to keep the economics going. That is one, very desperate, and deals became a lot more aggressive and a lot more very sort of -- if one of the assumptions was off by a hair, boom, but it worked in sort of our assumptions.

And with advent of the credit default swaps, that drove a lot of complexity and lot of issues with those deals because, A, they could be put together faster, and B, the hybrid transactions, hybrid CDOs came on the scene, and those were probably, in terms of their structural complexity, they were twice as complex as a normal CDO.

BY MR. BONDI:

Q In 2006, were there any internal complaints that you were hearing from your colleagues at Moody's concerning resources?

A Yes.

Q What complaints were you hearing concerning resources?

A There was not enough resources, we don't have enough time to do the deals, very much the deal flow was much greater than what we could manage with.

Q And who do you recall making those complaints?

A I am sure everyone at some point. We were working very hard compared to -- again, most people who joined signed up for the old Moody's where you could take a three-hour lunch.

So some people were there 16-hour days, et cetera, but a lot of people, they were there because of the lifestyle, and so they were getting less pay because of the lifestyle, so they felt that I am being pressured more given what I am supposed to

be doing at a rating agency.

But I would say most people would complain about resources.

Q Were you complaining about resources?

A Sure. I tried to do it in a positive manner, but yes.

Q What kind of response did you get from management when you complained about resources?

A Usually "We know, we are working on it."

Q And what other complaints were you hearing at the time?

A I think people were concerned that they didn't have a good grip on the deals as they were flying by.

Q Do you feel that you and your colleagues had a good grip on the deals?

A With 20/20 hindsight, absolutely not.

Q Tell me why -- you mentioned hybrid CDOs. First of all, just for the record, what is a hybrid CDO?

A A hybrid CDO is a CDO that is

partially funded with cash and partially synthetic, and it could be any combination.

The typical, standard typical hybrid CDO, there are many variations, was a CDO that had a vast majority of its assets as credit default swaps, so it was synthetic. On the liability side, the super senior was unfunded, so it was synthetic, while the mezzanine notes were funded.

So what that introduced to the deal is, number one, the funded notes brought in cash into the deal. That cash needed to be invested in something which had a risk of its own other than credit default swaps. So you had collateral risk.

Of course, bankers would want to push an aggressive collateral arrangement, so you had to look at that collateral arrangement. That could vary from something as simple as a GIC, guaranteed investment contract, to a total return swap with a bank. So, how does it work?

The other question for the collateral is not just who takes the risk

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for the collateral, at what point. So if you had a pay-as-you-go credit default swap on the asset side, if that credit default swap required payment from the CDO to be made, where did that money come from? Who would take the risk?

So, let's say if you need to make a payment, a credit payment on the credit default swap, let's say for example you invested your collateral -- which nobody did -- into 30-year Treasurys, you may go sell the Treasury, but it is a fixed rate investment and interest rates had moved, you would have a market loss. Who takes that loss? Is it the bank? Is it the CDO? We try to make sure it's not the CDO. Whoever it was, it was not, it should not be the CDO.

But you had to go through all these contingencies, what if this, what if that, because obviously if the CDO didn't make that payment it is in default. So if it is in default, the whole deal is in default. It would have to be liquidated, and the mezzanine tranches would be wiped

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out, probably.

The other problem came with the super senior on the liability side, because again, once you have exhausted all the cash collateral that was put in by the funding mezzanine tranches, you are still indebted to make the payments on the credit default swaps. Where would that come from? Usually that came from the unfunded super senior, so now you are concerned about the credit of the holder, which before you weren't, the credit of the holder of the super senior. What happened if they defaulted? You don't, again, our philosophy was that the bank holders of credit default swaps, the buyer of protection, should take that risk.

But there were a number of variations of all kinds, and the complexity they had in terms of payment waterfalls. What happens if you have -- you know, in a cash deal you have a prepayment that is cash, so it goes to the waterfall bonds, it gets paid off, very simple. In a synthetic deal you have -- or a hybrid deal you have a

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synthetic senior, cash mezzanine bonds. If you have a prepayment on the cash bond, it goes to the waterfall. You can't just let it flow to the mezzanines because they are getting paid back before the super senior. So you have to go through this, okay, what if, what if. So the layers of complexity are tremendous.

Plus they may have wanted to do a short bucket in the CDO. So ability to short a CDS to usually CDOs sold protection if they were hybrids. What if they wanted to buy protection? How would that work?

So all these, again, added an enormous amount of complexity, so we were dealing with an explosion of sort of innovation, and I don't think we had the resources to deal with it. It would have been much better in 20/20 hindsight to say let's stop, let's think about this and let's figure out how we need to -- so that was the unspoken thing. You can't stop, you kind of run with the flow. You may be able to slow things down, but you have to ride with the

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flow.

Q Were any of your colleagues saying I can't rate this deal, it is too complex?

A I don't recall.

Remember, this is a working environment, so people tried to have a positive attitude: How can I do this? If analysts had a question, the whole idea is they would go to their committee chair. The committee chair would think about it, they would probably huddle up with other people.

So the attitude that drove us was sort of a can-do attitude. You could go to other people, you would talk it through, et cetera.

MR. BUBB: Were there cases where analysts felt like they understood the deal, but that it simply didn't pass muster and they said no, we are not rating it?

THE WITNESS: No. I mean, there was a couple of deals that went through which we tried to -- it was

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almost like we had an obligation to follow our methodology.

There were a couple of deals that we actually tried very hard to, because there was some gut feeling that something was wrong, but we would try to work within the methodology. The numbers still came up okay, and that was, you know, that was sort of a what do you do at that point.

MR. BUBB: Let me follow up.

In both your stints at Moody's, was there ever a case in which the groups said no to deal?

THE WITNESS: Well, yes, yes.

MR. BUBB: In those cases, since the bank had access to your model, presumably they had run it through the model already.

THE WITNESS: Uh-huh.

MR. BUBB: And it passed the model. How would it ever come to you and not pass the model?

THE WITNESS: It is usually

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something that's sort of an issue of first impression.

So the one deal I was able to say no to as managing director was the deal called Tigress. That was essentially a repackaging of the equity positions of a hedge fund called Magnetar. Magnetar was responsible for doing a lot of deals called constellation deals because they are all named after constellations. And it turns out they were shorting, those deals were shorting some bonds in those deals. There was a recent investigation that was done about this.

But they came to us -- I guess they wanted to get out of their equity position, sort of cash out of their equity position. They came to us essentially with a CDO of CDO equities, residual pieces, and that is a deal I said no to. And, you know, theoretically you can fend them off

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but there is enough there to say, look, this is, even though we have a model, this is new enough that the model just no longer fits or makes sense in this deal.

MR. BUBB: Was the collateral rated?

THE WITNESS: Some of it was not rated, and so then we would have had to rerate some of the collateral, go in there and rerate some of the collateral.

I also was concerned about equity, sort of in terms like long correlation. It is a term that means equity, residual pieces at the bottom of distribution benefit from high correlation because it is, it becomes an option. You either hit it out of the ballpark and you lose everything, but you don't have much to lose.

Equity is long correlation, so if you are -- and this is the argument I used to stop the deal internally,

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was that because equity is long correlation, a lot of these deals were done by the same hedge fund and they seemed to have a lot of overlap or underestimating correlations if we use our normal correlation grid in the CDO ROM model.

I was also concerned about incentives as well, because that is something, unfortunately, if I could go back, incentives was the biggest problem in this field, but in this case I was just concerned the hedge fund did all these deals, they take a residual.

At this point, you know, anecdotally, bankers would not tell us where a lot of this stuff went, but by '06, '07 the super senior was essentially retained on the books of the bank. The mezzanine tranches went into either vehicles controlled by the bank or another bank on swaps, they would swap collateral into an SIV, for

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example, or an ABCP, asset-backed commercial paper conduit.

The rest of the non-triple A mezzanine would go into CDO warehouses. All CDOs had a bucket, an allocation for other CDOs, so there was no real investors other than the equity, who theoretically was incentivized to make the deal go on, and here was equity trying to cash out of their position.

I thought that, really, if that started happening, then I think our attitude to step back at Moody's, rightly or wrongly was, you know, we offered advice to investors, but if investors want to take the risk, they are sophisticated investors.

So to that theory, right, there is no investors. It is just bankers doing their deals and equities cashing out, who, it is just us. And so that is why, that was the main reason I said no, but I used the correlation

argument internally to push it back.

I was asked to reconsider. I said no, I am not doing the deal.

MR. BUBB: Who asked you to reconsider?

THE WITNESS: I think my manager, Yuri Yoshizawa.

BY MR. BONDI:

Q What happened as a result of you pushing back on this deal?

A Nothing immediate, but I think -- you know, this is -- I pushed back, this is '07, and I started doing a lot of market unfriendly things. So I think it set up for my eventual dismissal from the rating agency after the events of September, which was probably like the last straw.

(Lunch break.)

BY MR. BONDI:

Q Mr. Kolchinsky, we were talking before the break about your experiences when you returned to Moody's in 2005, 2006, 2007.

A Uh-huh.

Q And we were talking earlier

before the break about the various models that were used. You had mentioned the correlated binomial model, you mentioned CDO ROM.

Can you explain what models were used when and for what?

A Okay. We talked about, in terms of setting the probability distribution, there are two components. There is the distribution itself, the shape of the distribution, and there is the correlation.

Before I left, I believe we were using the normal binomial distribution, and the number of diversity bonds, which is an applied measure of correlation, was set by this two moment calculator. Shortly after I came back -- well, I think while I was at Lehman I think the paper on the correlated binomial was published.

The difference between normal, correlated has a fatter tail, just nothing else. Distribution takes some of the, removes some of the loss from the hump, if you will, puts it on the tail. Think of it

as normal distribution, puts it on the tail. You have lower probabilities here, but you have higher probabilities in the tail where the triple A's would be.

Q Lower probabilities in the 50 percentile, more probability in the first percentile?

A Yes, further down, more rare events. Gary published this paper on the correlated binomial.

Q And by Gary, you mean Dr. Gary Witt?

A Dr. Gary Witt.

Then there is a paper about new correlations for structured assets, which was meant to apply just through the CDO ROM model, or theoretically could apply anywhere, but that was published. I don't think Gary was involved, Dr. Witt was involved with that; tangentially, you would probably know better than I would. I was at Lehman. It was published, and then as I was coming back and officially in the summer of '05, they took the correlations in that paper, in the CDO ROM, and applied it to cash flow deals through the correlated binomial as the distribution.

So there is some ways to do it; you know, you could have actually taken the actual distribution and put it into the model. At the time I think it was seen as something impractical because of the number of runs you would have to do. You would have to run at least a thousand passes through our cash flow model, which was very time dependent.

So in order to sort of limit it, you would just match, I believe -- Dr. Witt would be better -- match the first and third moments of the loss distribution that came out of the CDO ROM with a correlated binomial distribution with a hundred assets, and then you got out the correlation. That is the output from the CDO ROM.

And then you would then put that in a cash flow model, and you would create a correlated binomial with that correlation, and that is how you would rate the deal.

MR. BUBB: You didn't have to simulate the cash flow model because you had an actual distribution, closed form distribution going under it?

THE WITNESS: Well, yeah, there was a closed -- the probability was that it was a closed form distribution, and we ran that through.

So then you would take that, you would already have to run, let's see, we had five defaults -- we had five interest rate scenarios and we had six default timing scenarios, so that made 30. For ABS CDOs we actually did, tried to also vary prepayment speeds, so it made a total of 90 different scenarios. Everything was weighted, and that was part of the problem, everything was weighted.

But 90 scenarios, each one would be run in a hundred passes for that scenario, so actually -- I don't mean like raina (phonetic) pass, but you would have to run nine thousand

scenarios for the cash flow model.

MR. BUBB: Was this documented in any sort of methodological document?

THE WITNESS: There was a document that came out on the application of the new correlations and the correlated binomial to ABS CDOs, Michael Xie was the author, along with Gary, along with Dr. Witt.

MR. BUBB: And that was in '05, we think.

THE WITNESS: I believe it was in the summer of '05. It was right after I came back.

BY MR. BONDI:

Q Do you recall the name of that paper?

A No. If I had an Internet connection I might be able to find it.

MR. BUBB: We may follow up with you.

THE WITNESS: I am happy to send it to you without serving a

subpoena. It is public information.

BY MR. BONDI:

Q Mr. Kolchinsky, the models that you have described here seem to be critical for the ultimate rating.

A Yes.

Q And as the models changed, the ratings could change significantly.

A Yes.

Q Who was involved in approving the ratings, and what would go in -- excuse me, strike that. Who was involved with coming up with these models, approving the models and the various assumptions and inputs that would be used for the models?

A I think they have improved this now, but at the time, again like anything else, it was ad hoc and it was generally the folks in the business unit who made that approval.

Q Now, you say ad hoc, and at the time --

A There is no set procedure.

Today there is supposedly a

credit policy group that has to approve, independent of the business line, that has to approve all these things. I don't think they do a great job. That was part of my testimony, the first testimony, in the sense that they are heavily outnumbered by the folks in the business lines, and if there is a vote they get outvoted all the time. They don't really have a lot of power to do their job. But at the time, that was all done at the business unit level.

Q But you used the phrase at the time, you mean up until your departure?

A Up until they implemented this credit policy group, and I think that was '07, '08, post crisis. It was done post crisis.

Q Post your tenure?

A Post my tenure, at Moody's Investor Service. When they started I was still at Moody's Corp. on the Moody's analytic side, but I was no longer at the rating agency.

Q With respect to how these models

came about, how the inputs came about, you mentioned that the business persons were behind these. Do you know if the business persons ran different scenarios when they were coming up with the models to see how a CDO might rate under one model versus the other and which model might have came up with a higher rating?

A I am sure they did, yes.

Q You say that you are sure you did, but do you know for a fact that they did?

A Well, I will give you an example that is sort of from a more recent approach where it has to be documented now. A lot of stuff wasn't documented, but part of the, sort of my complaint or my submission with respect to Nine Great Funding. Let me see.

So they have actually -- here, I will give you an example. This is just an example I will show you. Now, these things would be done before, but they would be done sort of, you know, internally just to see what the impact is, but yet people did care what the impact was going to be.

So if you look at this, this is a memo entitled, written by the credit policy group now that it was official and it talked about the changes in the methodology. So this is how it is, you know, and it talks about a lot of things, how it came about. But, as you can see, there is this sort of a negotiation between the line of business and the credit policy group and --

MR. BUBB: CP is credit policy, LOB is line of business?

THE WITNESS: CP is credit policy and LOB is line of business. You can see there is a key to understanding of what the impact is.

MR. BUBB: So the credit policy group and line of business each proposed a methodology for rating this deal, or class of deals.

THE WITNESS: Uh-huh.

MR. BUBB: And which proposal was more stringent?

THE WITNESS: Credit policy, of course. Line of business proposed

triple A two to five notches, credit policy proposal, six to 11.

BY MR. BONDI:

Q And that is six to 11 notches down?

A Down, yes. This is what, this was -- you know, probably this wasn't formalized. Informal things like this occurred whenever methodology would change.

Q So what you are showing us, for the record, is a recent example of a methodology memo?

A Yes.

Q So it is a Moody's credit policy structured finance methodology update approval memo --

A Uh-huh.

Q -- from, it appears to be December 9, 2009.

A Actually that is a typo, because I got this memo in July. This is a typo. The actual effective date was actually in -- there is actually an effective date line item.

This letter was written, the memo itself was written in July of '09, so the

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committee couldn't have taken place in December, so I think the writer had a typo on the front of the date.

Q So the date of methodology approval is December 10th, 2008?

A Eight, yes.

Q And this is an example, what you are showing us is an example of some more recent memos that actually shows a comparison in different approaches to a methodology for rating a series of deals, types of deals?

A Yes, that is correct.

Q But during your tenure in structured products ratings at Moody's, these type of memos were not done?

A No.

Q And fact, I believe --

A They may have been put together on a piece of paper, but not this formally, not with an outside -- it would have been done internally, so you would ask some mid-level analyst, say, tell me what the difference is, and they might write it up,

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they might send to you in an e-mail. The level of the delivered product would be anything back and forth.

Q Now, Moody's had two significant competitors, one more significant than the other.

A Yes.

Q S&P and Fitch.

When ratings methodologies were being developed during your tenure, do you know if the business personnel at Moody's would look to compare how Moody's proposed methodology might match up to, say, S&P or Fitch's methodologies?

A I don't think directly.

Well, a couple of things. First, at Moody's we didn't really have business managers in the sense that they were powerful. The managing directors in the group were effectively the business managers. You were supposed to manage not just the methodology but also your business line, so there is no separate role. It was, I believe they have been separated since,

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but it was the same role.

There was a business analyst who is on that e-mail whose role is more junior, more in a bookkeeping type of way, but you had to run your own line of business.

So I don't think it was done explicitly, but I am sure people had that in mind, what does this do vis-à-vis my competitive advantage versus the other rating agencies.

Q Now, shifting gears in the time that we have available, you mentioned synthetic deals earlier, synthetic CDO deals.

What were the challenges or concerns that you had with respect to rating of synthetic deals?

A Me personally or the whole group?

Q You personally, and then we will get to the question of the whole group as well.

A I think there was a lot of challenges that were addressed with the deals. A lot of them had to do with counterparty risk and collateral risk.

Counterparty risk means you don't

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have cash, you are dependent on another party, and that party may default. Even if that party, the default of that party doesn't cause you direct economic damage, for example, if that party was a protection buyer, the problem is the way credit default swaps worked is that once a party defaults, you have to mark everything to market.

And CDOs are ultimate trading vehicles, they are not really intended to take market risk. So you have to, the default of the counterparty could, A, cause direct economic loss, and B, cause you to have to unwind the deal. So those were counterparty risks.

The other big risks were collateral risks, because some of the tranches still had to be funded, and collateral used to fund still had -- any collateral could have risk, it could be market risk, it could be credit risk. How do you deal with those risks? So those are the things that added challenge, obviously. As a result of these deals, the complexity of deals increased.

My personal worry about synthetics was the correlation introduced in the market. Remember, I am thinking from a CDO point of view. Because you are able to replicate any number of credit default swaps, there is no sort of control, sort of having limited assets for different pools.

So when your only source was a cash asset, there was a natural limitation of diversity between different pools. You could only buy what you could buy. If you are ramping up at the same time, maybe you had some more pools, but if you didn't, you couldn't.

Now, with credit default swaps that limitation was gone. Anybody can do the same pool over and over again, stamp, stamp, stamp. The correlation between the deals increased, and we did write a paper about that. I think one of the e-mails that the Senate permanent subcommittee on investigations released had to do with that.

So that was, you know, one of the

things. I wasn't one of those people who predicted the market was going fall, I was not that smart. Where I thought my expertise was and the more I tried to figure it out is that at the level of incentives, what are the changes in the market due to the dynamics within a deal like this? What happens if all of a sudden you are not limited by actual cash assets and you can pick any portfolio you want? What does that mean to correlation between ABS CDOs and the next generation? So those are the kinds of things that worried me about synthetics.

The other thing we were worried about was, did we model them correctly, because even though they are pay-as-you-go they didn't exactly mirror the cash assets. So there were two types of credit default swaps. One was fixed cap, this is on CDOs, was fixed cap, I believe one was fixed cap and implied writedown, the other one was variable cap, no implied writedown.

I don't think we ever figured out what that means for a CDO. I mean at the

end of the day, because the underlying collateral, the underlying reference obligations subprime was so bad, I don't think we saw the impact that it had, but I don't think we ever figured out what it would be. It all blew up equally, so we didn't have that sort of middle part to find out what those differences applied to the deals. It was go, go, go.

The whole idea of stopping, saying let's figure this out before we go forward, that was just not an option.

Q With respect to how Moody's went about rating the cash CDOs and synthetic CDOs, can you just describe and list all of your concerns with respect to how Moody's went about rating cash CDOs, synthetic CDOs? Just list out your concerns so we can get them in one place.

A At one point or another I was concerned about correlation, what the ability of having synthetics did to the correlation assumptions; assuming, which I was wrong, that the correlation assumptions

before were correct, which turned out to be incorrect. I assumed the base correlation assumptions were correct, but what does that do, what does that do to our deals if the synthetics went up? So I was wrong in the correlation.

Having, you know, like I said, most CDOs went, sold protection over a long credit risk, but they all had short buckets, an ability to buy protection. How does that change, especially in terms of netting and cash flow payments? Let's see.

Oh. One of the biggest battles, and this was '07, was with the discount purchase rule. Remember, we talked about the discount purchase rule was intended to sort of get managers, bankers, not to buy things that were so -- we always realized, you know, that ratings moved slower than the market. Even at best, ratings will always move slower than the market. That is how they are designed, just like banking regulations, like any sort of quasi-regulatory events, move slower. So this was

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intended to sort of put a floor under how much arbitrage people could do.

And this was a rule that was on the books for a while, and it became sort of inconvenient when the ABX started blowing up. And we said, well, we want to make sure that the names going into these new deals are not discount obligations. So the bankers said we didn't know it applied to synthetics. I said I am not sure why it wouldn't, it is an asset.

And the problem is, unlike a cash bond which has one degree of freedom which is price, credit default swaps have a number of degrees of freedom. So identical economics could be delivered by an up front payment. So you could structure a credit default swap that has the same spread as a cash bond and an up front payment to reflect the price, or you can do it in the spread, or you can do a combination of both to change the yield. I can adjust the premium, adjust the up front payment to make it what I want to make it. You can change the

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reference price, you can do a lot of these things to achieve identical economics.

So with this kind of purchase we said okay. At that point we need a discount purchase, we say they are not really traded so we can't get prices. And it is difficult if you are trading -- at that point they were still trading on spread, not up front, most of them trading at spread, not up front payments. It is difficult because you need to have the life of the deal, which could be anything, in order to get a price.

So we said okay, they don't trade and they trade on spread. What we will do is that if the premium on the credit default swap is -- I forgot what we said -- a hundred basis points wider than the premium, the spread on the cash bond, then you will have to take that name, basically have it marked up in the market by X number of dealers, and use that as the discount purchase hurdle.

And at that point the game started being played. I saw one portfolio

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an analyst brought to me -- I think if our hurdle was a hundred, sort of if the test to get it marked to the market was a hundred basis points over the cash bond, I saw one portfolio, every single bond was 95 basis points over cash, 95 basically, specifically done because you can also do a portfolio trade.

You could say I will take some risky names that are out there, I will take some safe names, I will average the premium on each default portfolio. You had all these degrees of freedom to sort of avoid doing that.

So that was, I had a lot of bankers call me up and say -- this is in May of '07 -- this dislocation of subprime, it is just the market overreacting, everything is great. By the way, don't you still have them rated B double A, so why are you -- but I stuck with it, and I am not sure how successful I was because we had no way of monitoring it, but I stuck with it nevertheless.

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MR. BUBB: You stuck with this rule.

THE WITNESS: The rule, yes.

And when they still wouldn't do it we said, you know what? We will do it ourselves, because the key element is the weighted average life, so we will say fine, we will take the premium minus the spread, multiply it by the life, and we will get the discount to the price, and we will use a seven-year life as a random, and then if that meets the discount purchase, then we will use that.

So, it was just a lot of these games being played by bankers.

MR. BUBB: And were bankers successful at avoiding marking their CDS to market through changing --

THE WITNESS: I would assume some were. We tried very hard, but we had no market price access, so we had no means of knowing how compliant they are or where else economics could change.

MR. BUBB: What about on the cash side? Was it possible --

THE WITNESS: Just price, price is price.

MR. BUBB: And they reported, the bankers reported the purchase price to you?

THE WITNESS: Yes. It reported to the trustee. It was in the rules, so the trustee on a monthly basis -- it is for the accountants on the closing and the trustee on the periodic basis had a role of making sure if it is purchased below a certain price, that is how -- these were all rules in the indenture, the legal documents.

MR. BUBB: Do you believe it was possible, do you believe that bankers were able to game that rule on the cash side via --

THE WITNESS: No.

MR. BUBB: -- fraudulent reporting or any sort of manipulation

of the purchase price?

THE WITNESS: It is possible on the cash side that they would use, they could theoretically use a package trade in order to cover up the discount purchase and collude with the banker, I will sell you this, you sell me that, and you will pay me less, I will -- you know, kind of even up; the economics are the same, but you hide the fact that that was done on a discount purchase. That was not possible for us to monitor.

BY MR. BONDI:

Q You described games that bankers were playing with Moody's. What games were being played inside Moody's to ensure that deals were being rated or to ensure that ratings were coming out a certain way?

A I don't think I am aware of any games. What I have said is I think what people did wasn't so much commissions as much as omissions, and sort of my hard-earned lesson from this is that

statistics is an art, not a science.

So if you wanted to basically get comfortable with any kind of a financial model, you could. What kind of data you used, what range of data you used, for example, in lot of these simulations, people used Gaussian Copula simulations.

Now, the disadvantage to a Gaussian Copula, it may be okay at the individual borrower performance, but because what you were doing is you were taking effectively derivatives of that performance, small thin slices, I think it was harder to argue that if the mortgages performed like Gaussian Copula, that if you are measuring correlations of tranches on a mortgage deal, they also follow the Gaussian Copula.

Because, look, on the one hand everybody used Gaussian Copula at every level, but if you were to actually run the numbers up, which I did too late after, afterwards, you don't have a Gaussian performance, you have something that looks like a beta distribution or something that

looks like a different distribution, which what is the point of implied more losses at the tail of the risk.

But that is a shortcut that everybody took. No one I know questioned that Gaussian Copula. Everyone ran Gaussian Copula at every level regardless of the levels implied in the underlying, in their underlying asset, everyone on Wall Street, every rating agency. Part of the reason is the Gaussian Copula is a very simple simulation and people know how to do it. It is easy to do. Anything more than that would have required lot more processing, and it might have required you not to rate deals.

So people said, I think a lot of times with those kinds of things, it wasn't people knew what the answer was, they just didn't ask the question. It was easier not to ask the question because things were coming out okay.

Q What happened if an employee within Moody's raised concerns? Were the concerns addressed by management? And what

concerns were you hearing?

A We tried to address them. Most of the concerns we heard were about resources, time and pressure from the bankers. I don't recall that many sort of this is wrong kind of concerns. I think, rightly or wrongly, we were sitting at the top and nobody really questioned the ratings that were underneath.

I mean when I raised my concern in September, I was let go. But I was also a senior person, so I could be problem if all you want to do is do business. The more junior person, they would probably be pooh-poohed and don't worry about it.

It doesn't mean that none of the problems were addressed. You try to address it, but at the same time it's sort of a can-do attitude.

Q Tell me, what were the circumstances surrounding your departure from Moody's?

A Moody's Corp. or Moody's Investor Services?

Q From Moody's Investor Services.

A This is in '07. I was managing director in charge of the ABS CDOs.

The RMBS had not taken a huge amount of rating action. They had a small rating action in July, I believe, of '07. That was large at the time since we had 300 tranches, but most of the tranches they downgraded were originally at a BA level, while most of the reference obligation CDOs were B double A level, so it didn't really have much of an impact.

And finally, as the ABX, which tracks the prices of B double A tranches, triple A tranches, was declining, they were essentially forced to act. I believe they had a theory at the time that a lot of the delinquencies had to deal with mortgage fraud and that aggressive modifications would cure that problem and everything would go back to normal, so why change anything.

So I think there was more rationalization. I am sure part of it was business-based and part of it, I think

people just stuck their heads in the sand, really, created all these deals and they are just horrendous. It is so much easier just to close your eyes, close your ears and pretend nothing is going on, and it is bad for business too.

So they didn't do anything, but they sent out a survey to servicers to see what levels the modifications are occurring. It finally came back, basically no one is modifying any loans, so that sort of, that was the end of that fig leaf. You hung your hopes on modifications, nobody is modifying. So somebody I think forced them to take action.

This was -- I found out about it in September '07. I was told by Nicholas Weill that it was going to be across the board '06, it was going to be severe.

Q Could you spell Mr. Weill's last name?

A I believe it is W-E-I-L-L.

He told me that, and I still had deals that used those ratings as a basis for

my ratings. So, as we talked about before, you know, besides all these correlations, anything else, the biggest driver is the credit quality, the mean of that distribution.

So what he is telling me is the deals that I was still working on, these ratings were all wrong. He just needed time. It was an understaffed group -- I think he had three people -- he had to go through each one of these deals. They ended up downgrading 3,000 tranches.

At that point he decided all those ratings were wrong. I don't know if that is because I am a lawyer or what have you. I said, well, if I know those ratings are wrong, I can't assign new ratings based on those ratings. That is like a definition of securities fraud.

MR. BUBB: New ratings for what?

THE WITNESS: To the CDOs that are in the pipeline.

So I had these CDOs in the pipeline. This was after -- what happened after Bear Stearns funds collapsed, the pricing in the CDO world dropped. Most of these CDOs, either on a negative basis, they were in the trading book, not in the hold to maturity book, which means they were price sensitive. So banks had to all of a sudden mark all these things to market after Bear Stearns.

Panicking, they wanted to close the deals, and bankers were yelling. And I actually wrote -- there is an e-mail in the Senate, which I didn't give them, I guess it's from a management e-mail, because I had analysts coming at me every day, and the bankers, yelling and screaming they want to close, and I said no. At any time you have to follow procedures, at a very minimum you have to follow the very basic procedures.

So this was a very aggressive time for bankers that were pushing. I found out that all these ratings in my

deals are wrong, and they could be significant. We did a basic analysis for one deal, and the lowest triple A dropped I think to BA, so below investment grade, so a significant effect.

And I went to my manager, I said we can't do this because they are going to downgrade, it will be in violation of the law if we rated it. She didn't want to do anything.

MR. BUBB: Who was your manager?

THE WITNESS: Ms. Yoshizawa.

And I think she was concerned about market share, I think she was concerned about if we are not cooperative in these deals. She still had a healthy CLO pipeline. But I am speculating here. None of this was communicated to me.

So I went to Andy Kimball, who was the chief credit officer at the time through Dr. Witt. Well, what actually happened was -- and I don't

know how Gary, Dr. Witt remembers it, but I just didn't know what to do. After she said no, I didn't know what to do. I was sitting there going like I can't violate the law, I know this is wrong, I can't violate the law. I can't believe she doesn't want to do anything.

Either Gary walked by or I went to talk to Gary, and I told him, asked his advice as my manager, and he said why don't you talk to Mr. Kimball, the chief credit officer, because he was being very active and very basically fighting the good fight.

And I asked Dr. Witt if he could sort of intermediate for me, because I know if I do that, given sort of the culture at Moody's, I would be ostracized, so I didn't want to -- I was going to do it, but I didn't want to do it and not get it done. I wanted to at least have a fight if I was going to put my career

in jeopardy.

Mr. Kimball was interested. We had a conversation I think on the 18th or 19th of September. I told him about the problem, I told him about -- I believe he was aware of these incoming downgrades. My guess is he was pushing for them, and what that would mean to CDOs.

A few days later I was asked by my manager, she reversed herself, to draft a press release on adjusting the ratings on subprime bonds going into CDOs.

MR. BUBB: I am sorry, a bond manager you mean?

THE WITNESS: Mrs. Yoshizawa. So she completely reversed herself, and I believe that was through the efforts of Mr. Kimball.

MR. BUBB: When you initially raised the issue with Mrs. Yoshizawa, did you propose a solution to the problem?

THE WITNESS: I did. I thought we should stop until the, stop writing deals announced until the downgrades took effect.

MR. BUBB: And if she had adopted that solution, what would have been the impact on Moody's revenues?

THE WITNESS: I think they would be reduced. Not only would we not rate those deals -- what happened with Tigress when I said no, they went to Fitch, got it rated by Fitch. So it would be a direct hit.

But I think her biggest worry wasn't on these few ABS CDOs because at that time it was clear that product at the least going was to take a breather. It was on the other more lucrative or remaining lucrative product, which was the CLOs, which were done by the same bankers.

So I believe, and I am speculating here, her concern wasn't necessarily the direct loss from

missing a few deals, but her concern was in upsetting bankers who are providing her other remaining product.

The CLOs continued being issued for another year. So that is what I would speculate her concern was.

MR. BUBB: And what was the solution that ultimately was adopted?

THE WITNESS: I believe the solution that handled the securities fraud problem was to notch -- I think I might have a press release -- was to notch any subprime bonds going into CDOs by a number of notches, lower the notches, to sort of, to cover that risk.

BY MR. BONDI:

Q And that notching was for RMBS that was issued by Moody's?

A Yes. I should -- unfortunately I didn't bring -- I have, at home I actually have all these things in nice little envelopes.

We did at Moody's a press release.

MR. BUBB: We can find the

press release.

THE WITNESS: I would look for it on like a Lexis-Nexis. I don't think it is on the web site any more. That is where I found it.

BY MR. BONDI:

Q Mr. Kolchinsky, I have a few questions from your testimony before the permanent subcommittee on investigations from last week.

You stated in your opening statement that it was, quote, "easy to avoid questioning whether the collateral provided by the bankers was really of the same quality assumed by the model, whether collateral standard declined or whether some of the parties had ulterior motives in closing a transaction," end of quote.

A I was directly addressing the, I guess the whole short sellers, Paulson kind of thing. We didn't know about Paulson at all, but what I told the permanent subcommittee on investigations after that came out, I actually thought a lot about it.

And it mattered to me because it changed the dynamics, it changed -- you know, the example I give, you know, you are building a house, you are contracting, you find out that the architect is a person who wants that house to be blown up. You can check the architectural plans, it may be they look okay, but do you really trust that architect? You know what? I want this house to fall down as quickly as possible. Here are the plans. Here's a full disclosure of the plans. Do you really trust them? No, you don't. Would you use them? No, you wouldn't. Even if they looked okay, would you take that risk? No. So it is a qualitative versus quantitative, and that is what I meant by that.

Q In retrospect, are there any particular collateral managers now that you think may have had an ulterior motive, aside from John Paulson?

A Not collateral -- well, this is hearsay. Is it okay if I --

Q Sure.

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A -- give hearsay?

Hearsay in the market is that, and this was I think also mentioned by Morgenstern, that Tricadia shorted into their own deals. They are both the manager and shorting collateral into their own deals, so that was in essence where the actual manager was on the one hand saying as a manager I have a fiduciary duty to, knowing all this, to maximize values, shorting collateral into the deal, using the CDO as a vehicle to short subprime.

That was the only collateral manager. In terms of what Magnetar, that trade, Magnetar spurred a lot of these managers to just put their names on deals, and one of those managers is Harding did a lot of deals.

Q Harding?

A Harding Advisory. If you read Michael Lewis's book, the president's name was Wing Chau. There is one scene in Michael Lewis's book where one of the hedge fund investors, Eisman, meets with Wing Chau

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at a conference. He doesn't come out very well in the book, Mr. Chau does not, in Mr. Lewis's book.

Here's the press release. It says given a sort of -- by vintage and by original rating. So for the second half '05 vintage, anything rated double A rated would not be adjusted, single A rated would be adjusted by one notch, and B double A rated would be adjusted by two notches.

The first half of '06 vintage, same categories as one, two, four, again based on ratings, and for second half '06, first half '07, same categories, two, three, six. We take that adjustment to the CDO when we figure out the average credit quality of the portfolio.

Q Tell me, during your tenure as a managing director, who were your points of contact for CDOs at Merrill Lynch?

A Cecelia Pan.

Q Citigroup?

A It was various. They didn't have one coordinated person. It would be --

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gosh. I know one person, Scott Surek, but they had a lot of folks, so I would go back and forth.

Q Do you deal with Nestor Dominguez?

A No. We didn't deal at that high level. Rating agencies were, as far as the securitization food chain, we are above the accountants, maybe on par with lawyers, but --

Q Darius Grant, does that name ring a bell?

A I know the name, but no.

Q What about at EBS?

A Again, sort of at the VP director type level, give me some names, I will tell you yes or no.

I will tell you, I kept all the, as managing director I had to essentially staff up transactions. This is something I am happy to provide.

Q One thing we will follow up with you off line, Mr. Kolchinsky, is the names of your points of contact at CDO issuers and any managers who you may have dealt with.

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A Sure.

Q Also, we may want to follow up with you to see if you have contact information for other former Moody's employees. We can follow up off line.

One thing I did want to close the loop on, which I didn't think we did, is about what ultimately culminated in you being asked to leave Moody's Investor Services?

A Well, after that, after going to Mr. Kimball, Mrs. Yoshizawa started excluding me from things. This was obviously a huge time for ABS CDOs, but there were meetings that I wasn't called to.

It was sort of clear that she wasn't very happy with me. It sort of started getting more and more, and by the end of October she asked me to leave the group. She came by my office one night and said there is no room for you any more in derivatives; if you can find another position at Moody's, that is fine. She said my old manager Gus may have a position for

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me, you should go talk to me him, but there is no more room for me in derivatives.

MR. BUBB: Did she explain to you why you were being asked to leave?

THE WITNESS: I believe the standard reason is that there was a reduction in force, and that was part of that reduction in force. I believe it was because I went over her head.

They also hired another managing director about ten months later. They promoted somebody in a market that was significantly worse than it was when I left. So it begs the question, you know, if you let go of somebody because there is no business, why are you promoting somebody else into the identical role when business is worse?

But this is, I do have a disclosure. I do have a Sarbanes-Oxley complaint that I filed.

(Discussion off the record.)

BY MR. BONDI:

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Q Were you involved in rating a deal called Vertical ABS CDO 2007-1? UBS was the issuer?

A Not directly. Again, this was rated underneath me as managing director.

MR. BUBB: Could we clean up one last thing? After your manager asked you to leave the CDO group, where did you go?

THE WITNESS: I went to work for my old manager, Gus Harris, and they were going to buy a small pricing, evaluate a pricing service. I was going to run that.

The position was not budgeted at the level -- it was really meant to be run by a VP, SVP type level, not a managing director, so I had to take a pay cut. But, you know, I figured it is what it is. And, you know, I was happy that Mr. Kimball was able to change the direction. I thought that maybe Moody's was going to turn over a new leaf, and so I said, you know, it

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is water under the bridge, let me just try a new endeavor.

MR. BUBB: When did you leave that job?

THE WITNESS: I actually did something else for Mr. Harris in structured finance evaluations, but I left Moody's Corp., Moody's analytics in September '09.

MR. BUBB: Why did you leave Moody's Corp. employment in September 2009?

THE WITNESS: This is related to the Sarbanes-Oxley filing. I filed a complaint with our internal compliance group, which I believe you have a copy, I think you are looking at right here, related to transaction called Nine Great Funding Two.

Sort of the long and short of it, I could go through all the details, but they hired an outside law firm to investigate.

MR. BUBB: Investigate your

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complaint?

THE WITNESS: Supposedly. I believe they were investigating me, and I can explain why.

MR. BONDI: Was the law firm Kramer Levin?

THE WITNESS: That was Kramer Levin, yes.

My understanding, I don't have proof, is they were hired by Sullivan Cromwell, so basically they are sort of, you know, local counsel for Moody's, and they wanted to speak with me.

I said yes, I would be happy to, but I am represented by an attorney, and as you went through the whole speaking, that was not a nicety they went through. I said -- well, the way it happened is I said, look, I am represented by an attorney, I would like to have her with me, could you send us an agenda so we can prepare for the meeting? At first Kramer Levin said yes. We set a time for the

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meeting.

A week before that I hadn't still received the memo, so I called them and asked is there a memo coming? And they said yes, we will get it on -- this was like a Thursday or Friday of the last week of August -- you will receive it that Monday, which was August 31st, and we agreed to get it in the morning so I would have time to speak with my attorney.

MR. BUBB: The "they" is Kramer Levin, attorneys at Kramer Levin?

THE WITNESS: Yes. They shouldn't be talking to me in the first place as I am represented, but they should at least give Jenice a call, and they knew about Jenice. I told them about Jenice

MR. BUBB: Jenice is your attorney.

THE WITNESS: Yes, my attorney, Jenice Malecki.

MR. BUBB: So they said they

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would send the memo by August 31st?

THE WITNESS: Yes, Monday, August 31st in the morning.

That morning comes and goes, there is no memo. I called them up and -- actually I sent them an e-mail saying we need to postpone the meeting until I get the agenda. I got a phone call from the partner, senior partner Barry Burke. He says we can't put anything in writing, can we talk about the agenda? I said okay, let's talk.

Nothing during that conversation convinced me that they were actually doing any real investigation of -- one thing, here's, you know, I believe it's sort of more the Department of Labor. I was not involved with any of this. All of this memo was built on -- so I had no personal knowledge of any of this.

MR. BUBB: The Nine Great Funding deal.

THE WITNESS: Right, no

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personal knowledge. It was all built on committee memos and all the required paperwork that the rating agency is required to do.

All the paperwork was in the possession of Moody's Investor Services, so there is no, nothing I could give them, no personal information I could give about this deal. Everything was, as you saw, documented in terms of that memo, committee memos on each of the downgrades on each of the deals.

I told them that. I said you have all the documents. They could have sent me questions, but if they couldn't find something they could have said where is this fact or that fact. They didn't want to do anything like that. So I said, you know, I am still not convinced, please send me a memo and we could sit and do a meeting. So that was Monday.

On Thursday, I get called by HR

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into their office. It was -- I got suspicious, so I actually turned on the recording portion of my iPhone, I had it on record. But it was, the HR person, it was one of the associate general counsel for Moody's. I am not recording now, by the way.

And we talked about why I didn't want to speak to counsel without an attorney. And they said, well, if you don't -- Mr. Burke, who was the senior partner from Kramer Levin, he is here now, we want you to speak to him right now, or you are suspended.

And I said look, I have an attorney, I would like to have my attorney. No, you are going speak to him now or you are suspended. I mean, I can play it for you if you would like. I have it here; at least the pivotal moments.

BY MR. BONDI:

Q Why don't we talk about this off

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line?

A Obviously this is not your, this is more -- I think it is for color for you, not for --

Q Why don't you describe what was said for the record, but don't play anything?

A I don't remember exactly, especially since I have it recorded, but we talked about -- my concern was, because if you look at the addendum, even after I put this complaint in, nothing was done. There was another further substitution in the deal.

So I said you know what? I was concerned that this was either going to be sort of a whitewash, basically. They are defense counsel. They are hired by Sullivan Cromwell, who was already outside defense counsel for Moody's. They represent -- Sullivan Cromwell I think at that point represented Michael Kanef, who was the addressee in this memo as an individual. They were defense counsel.

So I just wanted to make sure -- I didn't see a reason for the interview

other than something, that it was to punish me, or something not right, because I didn't have any personal knowledge. It was all documented and they had complete possession and control of documents.

They could have also asked me something, as we are talking now; you know, we don't get this part, why do you think this is the case? Well, I could have said this is why. None of that was, the only thing they wanted to do was to talk to me, obviously without my attorney, so I said no.

They said we want you to speak to Mr. Burke now or you are suspended. I said fine, I am not speaking to him. I was suspended.

Q What is your current status?

A I am no longer employed by Moody's. It's, I believe I was technically terminated, I forget what the legal term is, by Moody's.

Q When?

A I sent an e-mail, I don't know if I have it here, I sent an e-mail to Moody's

stating that their actions prior to my suspension and the suspension itself was a -- it is not a technical termination, but I was effectively terminated.

Q Constructive termination?

A Constructive termination. They asked me to return all my Moody's equipment. I was taken off, immediately off the internal and external directories from my friends at the firm. My office was locked and quarantined. It was very clear that I was not welcome back.

Q And what did Dr. Gary Witt do after this happened?

A After?

Q After you were suspended?

A Dr. Witt was already a professor. He had left Moody's at that point.

In '07 -- we talked about it, but then we just went on with our lives. Again, in '07 I thought that the rating agency -- my sort of 10,000-foot view of it, I think, and I say it in my testimony, I think prior to the crisis there were people, I believe

genuinely honest people, who held the view that we should be able to rate anything and put a number on anything, and it makes sense in some cases. You are a credit specialist, that is your role. So that afterwards, I think the whole quest for market share changes the whole dynamic of it.

To be honest, I don't know what question you asked that I was answering. I think I went on my own tangent.

Q Let me be a little bit more specific.

After you were removed from Moody's Investor Services, did Gary Witt resign over it?

A Uh-uh, I don't believe directly, no. I wouldn't have asked him or -- I think we talked about it once. I don't know -- let me step back.

To my knowledge, no. I think at that point he'd had it with Moody's, so he was ready to leave.

Q Senator Levin asked at the hearing last week if -- he asked several of

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the witnesses, but I don't believe he asked you this question, so I will ask you, is: Do you know of anyone taken off of a deal or taken off of the next deal because a banker didn't like the Moody's employee and the scrutiny that a Moody's employee might be applying to a deal?

A Yes, the answer is yes.

Q Who?

A Rick Mickalek was certainly banned from working on some deals. This was sort of my understanding. It wasn't when I was a managing director. My understanding, he wasn't allowed to work on some deals.

Q Anyone else?

A Not that I can remember.

You know one thing, there is an e-mail in there that was addressed to me from Alexander Reketa about a -- it was an e-mail that, in the documents that were released by the permanent subcommittee on investigations -- there was an e-mail to me from Alexander Reketa, who was then the head of CDOs at Mizuho. He had, effectively that

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was one of those e-mails that people ask to take somebody off the next deal. This was regarding an analyst named Sindhu Veluri, and it was his excuse that she wasn't experienced. And during my testimony I actually -- I don't know if you recall, I actually said that, I tried to defend her because she was actually a very good analyst.

I don't recall if I didn't assign her on the next deal with them. If I didn't, it wouldn't be because he asked me to. It was because she had her hands full doing the other, the transaction that, this transaction, which she was staff on as well.

But those kinds of requests came a lot. I try not to react to them. I don't think I ever have, to be honest with you. But obviously Rick was big example of someone who was known not to be allowed to work on certain deals.

Q And Rick is?

A Mr. Mickalek.

Q We were talking earlier about the

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Vertical ABS CDO 2007-1 which was issued by UBS?

A Yes.

Q Who was involved at Moody's in that deal?

A I would have to look up my e-mails. I don't recall.

Q What e-mails are you looking up? E-mails that you took with you?

A I have e-mails -- whenever we created a special sort of HTML-based software, which would generate staffing e-mails, it helped us to manage the work flow. So I have kept all my staffing e-mails.

MR. BUBB: These were the HTML software output that was outside of your standard e-mail system?

THE WITNESS: It generated e-mail. It was just -- here, this is what it looks like. It just had some data that just basically allowed us, there was some pull-down menus.

Instead of generating what was

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done before, these e-mails were generated by typing. All this basically allowed you to do is quickly put the names in, click, send. It would just update and it can access database and it would send out the e-mail to the staff in question. It was just a word flow tool, that is all.

MR. BUBB: And were those e-mails routinely deleted after some period by Moody's?

THE WITNESS: I think Moody's has a, had a document preservation policy which requires that documents are deleted after a certain time.

Here's the original. I don't know if this changed, but here's the original staffing e-mail for Vertical '07. I have Saiyid Islam as the quantitative analyst, Peter Hallenbeck as the legal analyst. I guess I was the committee chair.

That is it. That is the contact at UBS. You asked me who was

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my contact, Vab Kumar was my contact. Here, if you want to take a look at it. This is pre-automatic generation, so this was all created by hand. So we just basically created a software that mimicked this but didn't force us to write every line.
MR. BUBB: Why didn't your e-mails get deleted in accordance with Moody's document preservation policy?
THE WITNESS: Because I kept all the e-mails, archived them.
MR. BUBB: You archived them separate from their automatic deletion process?
THE WITNESS: I think at some point they stopped auto delete, but I would periodically archive all of my e-mails out of -- I did it out of necessity because the size for the in box, the live in box, was so small it would get overwhelmed after a few weeks, so by necessity I got into the habit of periodically moving e-mails

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out of that live e-mail box.
MR. BUBB: Did other employees archive e-mails in a similar manner?
THE WITNESS: I think so, but I also took them home, which made the difference.
I would imagine one or two folks also did the same thing. Basically this is the post word flow software output, so it is more clean, streamlined, and I didn't have to, I just basically pull down boxes for those things.
But I have all these e-mails, all these staffing e-mails, so whenever I staff or anybody staffs a deal, I have these e-mails.
MR. BUBB: Were they provided to the permanent subcommittee on investigations?
THE WITNESS: Not these e-mails, no. But what I told them is I can give you what I think is critical to the level of the things

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that we talked about, but I have all this other stuff because I have lot of, you know, filler here as well. You are welcome to any and all of it.
I can even burn a CD with all the stuff; as I make the offer, with a subpoena I can burn a CD with this. Just there is a lot of not interesting stuff in there. You are welcome to all of it.
MR. BONDI: Mr. Kolchinsky, we would ask you to continue to preserve and maintain all of the e-mails, documents, electronic files, recordings, anything else that you may have --
THE WITNESS: Of course.
MR. BONDI: -- retained through the course of your work with Moody's. We will follow up off line with a subpoena for those additional, that additional data. Thank you.
THE WITNESS: No problem.
MR. BONDI: In the interest of

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time we are going to cut this interview short. We hope we can take you up on your earlier offer and talk to you occasionally through this process --
THE WITNESS: Of course, absolutely.
MR. BONDI: -- throughout our investigation. And we are cognizant of your time and perhaps we can follow up by phone in the future --
THE WITNESS: Absolutely, yes.
MR. BONDI: -- or during other convenient times for you. We appreciate you meeting with us in person.
THE WITNESS: No problem at all.
MR. BONDI: In the remaining few minutes, Tom, do you have any pressing questions?
MR. BORGERS: Yes, one real quick question.
Do you have anyone on the RMBS side who had early warning signs what

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was going on on their side because it was much earlier than your side of the CDO?
THE WITNESS: Yeah, they would have known more. Like I said, we --
MR. BORGERS: Do you have any names of those that might have shared some insight?
THE WITNESS: I don't know if they shared -- I can give you the names of some of the senior people I know --
MR. BORGERS: Okay.
THE WITNESS: -- that knew the product area better.
Obviously I would start with Mr. Michael Kanef, who was the head of the whole group; Nicholas Weill, still at Moody's; Warren Kornfeld, also still at Moody's.
Jay Siegel has left. His exit interview was in one of the documents that was released by the permanent subcommittee on investigations, and

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David Tiescher. There is a David Tesher at S&P also, but that's not -- that is different.
MR. BONDI: Is Mr. Tiescher still at Moody's?
THE WITNESS: I don't know. He was the nominal head of compliance who replaced Scott McCluskey, but he didn't do much. He didn't work on my issues either, and then when they brought in this new person as the head of compliance, I don't know what happened to David. I have no idea where he is.
MR. BONDI: Mr. McCluskey, if we could ask your help with the following: Could you go home and search your contacts for your colleagues from Moody's who are no longer employed with Moody's who worked with you on the CDO side or the RMBS side, and e-mail us a list of names and contact information?
THE WITNESS: Okay.

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MR. BONDI: It would be enormously helpful for us. We are trying to get in touch with former employees of Moody's.
THE WITNESS: I would guess you know most of them, but, you know, it is Mr. Mickalek who was on the panel, Mr. Sifuentes who was on the panel, Mark Frobea, who was not on this panel. But I can get a few more names.
MR. BONDI: That would be helpful. And if you could err on the side of giving us everything.
THE WITNESS: Okay. I may not have their --
MR. BONDI: Even persons who you think might not be directly relevant for our investigation, we would like to have a universe of the former employees --
THE WITNESS: Sure.
MR. BONDI: -- at Moody's. To the extent, though, that you believe

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some may be more relevant than others, please let us know who you recommend we speak to first.
THE WITNESS: Sure.
MR. BORGERS: Would you have an organizational chart in your archive?
THE WITNESS: No, not an organizational chart. It switched back and forth as well. I can sort of give you an understanding of how it is.
There is a current organizational chart that Moody's does send out on a weekly basis in structured finance. They have what is called a structured finance quick check. It is a spreadsheet, but one of the slides there has an org. chart of at least the structured finance unit.
MR. BORGERS: Okay. Thank you.
MR. BONDI: Mr. Kolchinsky, our investigation is confidential. We just ask that you do not discuss what we have talked about with anyone else

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outside of any lawyers who you may want to consult.

I understand for the record, sir, and I should have put this up front, that you are choosing to speak to us without counsel and that we have received the blessing of your employment counsel to proceed at your wishes to talk to you directly.

THE WITNESS: That is correct.

MR. BONDI: If at any time, though, sir, that you ever want to consult counsel or want to involve counsel, that is your choice and we will honor your choice to have counsel present, as I indicated prior to the e-mail, that you could have counsel here today, and you declined, is that correct?

THE WITNESS: That is correct. I also asked that as long as I am not the subject of this investigation; if that changes, please let me know.

MR. BONDI: Sir, we have no

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subjects of our investigation. We are fact-finding, as I said.

But thank you for your time. We will speak I am sure in the future.

THE WITNESS: Absolutely.

MR. BONDI: Thank you very much.

(Time noted: 3: 00 p.m.)

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CERTIFICATION

I, Jessica R. Berman, a Notary Public for and within the State of New York, do hereby certify:

That the witness whose testimony as herein set forth, and that the within transcript is a true record of the testimony given by said witness.

I further certify that I am not related to any of the parties to this action by blood or marriage, and that I am in no way interested in the outcome of this matter.

IN WITNESS WHEREOF, I have hereunto set my hand this 5th day of May, 2010.

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Jessica R. Berman

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