

Testimony of Charles Prince
Former Chairman and CEO of Citigroup Inc.
Before the Financial Crisis Inquiry Commission
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Chairman Angelides, Vice-Chairman Thomas, Members of the Commission: My name is Chuck Prince, and I was the CEO of Citigroup Inc. from October 2003 until November 4, 2007. I am pleased to be here today with my long-time colleague Secretary Rubin to try to assist the Commission with its important work.

Before becoming CEO, I held various positions in Citi's senior management, including the head of our corporate and investment bank (the job for which Mr. Maheras later assumed co-responsibility), the Chief Administrative Officer of the Company, and its General Counsel. Before that, I worked in a variety of other positions at Citi and its predecessor companies. For nearly thirty years, until November 2007, when I resigned, Citi was my professional life.

I have given a great deal of thought to the unique events that led to the financial crisis and which bring us here today. I wanted to share some of my views, which I believe are important to set the context for the problems that arose at Citi as well as many other financial institutions and eventually led to Citi's receipt of government assistance.

The financial crisis resulted from the confluence of several factors, the absence of any of which would likely have caused the crisis to be averted or significantly moderated. First was the unusually long period of low interest rates, stemming from a change in the pattern of global funds flows following the 1998 emerging markets financial crisis and the stimulative actions of the Fed following the bursting of the tech bubble and the terrorist attacks of 9/11. As a result, investors were reaching for yield,

and many people, from investors to traders to rating agencies to regulators, believed that a new era of generally lower risk had begun. During this period, securitized products as an asset class grew dramatically in an effort to satisfy investor demand for products that had higher yields but were still believed to have a high degree of safety. The growth in securitized products also reflected a growing belief in and reliance on financial modeling by traders as a basis for risk decisions and a growing reliance on rating agency determinations by investors. As a result of the rapid growth in demand for assets to be securitized, together with long-standing and bi-partisan federal policies encouraging the expansion of home ownership, the asset class of subprime mortgages grew very quickly. The patchwork nature of state regulation of the origination of subprime (indeed of all) mortgages led, in hindsight, to the origination of more and poorer quality subprime assets to be securitized. Eventually, the rating agencies dramatically downgraded their ratings on the securitized products collateralized by these subprime loans. The precipitous nature of the actions by the rating agencies, together with the widespread holdings of these securities, caused a broad and generalized freezing of the securities markets as investors could no longer be sure what standards and models of risk and safety could be relied upon and who held what levels of risk. This general freezing of the credit markets then precipitated a severe contraction of trade that led to the general recession that still afflicts us.

It is against this backdrop that the events at Citi (and many other banks and financial institutions) took place. Specifically, on November 4, 2007, Citi announced an estimated \$8 billion to \$11 billion in write-downs related to subprime-related holdings. That same day, I resigned as CEO. After I left, Citi incurred even greater

losses which led Citi to receive over \$45 billion in federal TARP funds. I can only say that I am deeply sorry that our management—starting with me—was not more prescient and that we did not foresee what lay before us.

As the Commissioners are no doubt already aware, the largest losses at Citi emanated from what were perceived at the time to be extremely safe “super-senior” tranches of CDOs that carried the lowest possible risk of default. It bears emphasis that Citi was by no means alone in this view and that everyone, including our risk managers, government regulators, other banks and CDO structurers, all believed that these securities held virtually no risk—a perception strongly reinforced by the above-AAA rating bestowed by the rating agencies. I am told that Citi’s write-downs on these specific securities totaled some \$30 billion over a period of six quarters, and that this factor alone may have made the difference between Citi’s ultimate problems and those of other banks.

While I was not aware of the decisions being made on the trading desks to retain these super-senior tranches, given the universal perception that these super-senior positions were extremely low risk, it is hard for me to fault the traders who made the decisions to retain these positions on Citi’s books. After all, having \$40 billion of AAA+-rated paper on the balance sheet of a \$2 trillion company would typically not raise a concern. Moreover, it is important to appreciate that the CDO business, which was only one very small piece of a very large and complex financial organization, was being managed by highly experienced traders and risk managers and was fully transparent to our regulators, who were imbedded across the Company. In retrospect, it turned out the risk assessment, while widely held, was wrong, given the wholly unanticipated and

dramatic collapse in residential real estate values across the board, in every community and geographic location nationwide (and across many parts of the world).

I always believed that the risk function at Citi was a critical part of our overall business. After becoming CEO, one of the first things I did was name David Bushnell Chief Risk Officer and change the reporting structure so that the risk function was completely independent of the businesses (which it was not before). The risk professionals were not paid based on profits, volumes or revenues of the business units, which I believed was good governance and ahead of best practices at the time.

Mr. Bushnell himself was known as one of the most sophisticated risk managers in the investment banking community, with a strong, hands-on trading background. I believe that neither Mr. Bushnell nor any of the senior bankers or traders understood the super-senior securities to have any material risk of loss until October 2007.

As serious issues unfolded in the late summer and fall of 2007 relating to the subprime market and our lower-rated CDO holdings (as well as certain other more significant businesses, such as leveraged lending), our senior management was fully focused on the unprecedented issues the Company faced. We had multiple special Board and committee meetings to apprise the Board members of the issues as they developed in real time and to solicit their valuable advice and counsel. Regrettably, we were not able to prevent the losses that occurred, but it was not a result of management or Board inattention or a lack of proper reporting of information.

The “lessons learned” from this experience are many. But let me address two issues that seem to come up repeatedly when discussing Citigroup: Is Citi “Too Big

to Fail?” And is it “Too Big to Manage?” These are separate but related questions, as you know. Let me start with the latter:

I personally do *not* think Citi was “too big to manage.” To be sure, it was a challenge to manage. But we made enormous strides during my tenure to improve the way in which the various parts of Citi interacted with each other, and I think the Company as a whole was better for it. In any event, I do not think that the broad, multi-faceted and diversified nature of Citi’s business materially contributed to our losses or to the financial crisis more generally—indeed, smaller, more narrowly focused firms suffered in similar ways. To the contrary, I continue to believe that Citi is a unique institution—it is the only truly international U.S.-based bank—a feature that gives it great advantages in many areas of its business and around the globe.

“Too Big to Fail” is a harder issue. My own view is that we are past the days of exclusively small, local-based banks and financial institutions. While these local institutions certainly have a place in the financial landscape, the financial world we live in is increasingly complex, interconnected and global, and I think this demands equally sophisticated, global and diversified financial institutions. That said, I certainly do not believe it is good for the United States to have a financial system where the failure (or threatened failure) of key financial institutions will impose the kind of dramatic and near-catastrophic damage on the entire financial system and the national and world economy that we saw when Lehman failed and when numerous other financial institutions, including Citi, needed extraordinary government assistance. We must find a solution to this problem, whether through resolution authority, greater regulation, increased capital

requirements or all the other creative and innovative measures that your Commission has been discussing.

I thank you for your time, and I am happy to answer your questions.

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