Global Balance Sheet

Overview of
Repo 105 (FID) / 108 (Equities)

July 2006

LEHMAN BROTHERS
Accounting Theory Behind Repo 105 / 108

- Summary of FAS140, "Accounting for Transfers and Servicing of Financial Assets"
  The transferor has sold assets if and only if all of the following conditions are met:

9 (a) The transferred assets have been isolated from the transferor...
9 (b) Each transferee has the right to pledge or exchange the assets and no condition constrains the transferee
9 (c) The transferor does not maintain effective control over the transferred assets

- Repo transactions are normally recorded on the balance sheet as financings. Under certain circumstances we get 'true-sale' treatment we get to treat the repo as a sale.

Legal opinion obtained from Linklaters (for LBIE)
A repo under a Global Master Repurchase Agreement [GMRA] is a 'true-sale'

For tri-party the Euroclear 're-use' option is active
For equity securities we ensure that voting rights have been transferred

Above normal market haircut 105% for Fixed Income and 108% for Equities
Additional haircut implies that we have insufficient cash to repurchase assets and therefore they are 'sold'

9 (a) 9 (c)
9 (b) 9 (c)
Example Flow Diagram

Original purchase

Intercompany repo to LBIE [no haircut]

Repo 105 to street

LBIE

$5 Derivative asset established as MTM on forward purchase
Operating Rules

- Trades should only be done on readily obtainable securities (Operating procedure requirement, not a GAAP requirement)
- Fixed Income securities executed with a haircut of 105% and equity securities of 108%
  - Re-use agreements are needed for triparty repo
  - For equity securities – Lehman gives up voting rights per agreement

- Repo 105 is capped at $17B (1 x leverage) [per Chris O’Meara and Ed Grieb]
- Repo 108 is capped at $5B [per Chris O’Meara and Ed Grieb]
- Repo 105 transactions must be executed on a continual basis and remain in force throughout the month. To meet this requirement, the amount outstanding at any time should be maintained at approximately 80% of the amount at month – end. [per Chris O’Meara and Ed Grieb]
Status of Legal Opinions

- Agreements are in place with the following organizations:
  - GMRA (Global Master Repurchase Agreement)
  - OSLA (Overseas Securities Lending Agreement) – never used
  - GESLA (Master Gilt Edged Stock Lending Agreement) – never used
  - GMSLA (Global Master Securities Lending Agreement) – never used

May 2001

September 2004

January 2006

May 2006

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Monthly Trend

- Total Repo 105 usage reached a record high of $21B for May quarter end
- Repo108 for equity securities was introduced as at May 2006 [$0.6B]

<table>
<thead>
<tr>
<th>REPO 105 Month – End Trend</th>
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<tbody>
<tr>
<td>$ Million</td>
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<tr>
<td>Jan-05    Feb-05    Mar-05    Apr-05    May-05    Jun-05    Jul-05    Aug-05    Sep-05    Oct-05    Nov-05    Dec-05    Jan-06    Feb-06    Mar-06    Apr-06    May-06</td>
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<tr>
<td>13,600  13,007  12,816  13,090  13,696  13,364  14,610  14,612  13,128  14,310  13,173  12,199  21,046</td>
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Daily Trend

- Total Repo 105 / 108 usage has not been maintained at 80% Tangible equity intra month.
Business Benefit

November 2005
$14.6B

May 2006
$21.4B

- Nov 2005 Total Repo 105/108 Consumption
- Nov 2005 Individual BPM Consumption Expressed as a % of original Balance Sheet

- May 2006 Total Repo 105/108 Consumption
- May 2006 Individual BPM Consumption Expressed as a % of original Balance Sheet
<table>
<thead>
<tr>
<th>Company</th>
<th>Status</th>
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<tbody>
<tr>
<td>Goldman Sachs</td>
<td>✗</td>
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<tr>
<td>Merrill Lynch</td>
<td>?</td>
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<tr>
<td>Morgan Stanley</td>
<td>✓</td>
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<tr>
<td>Bear Stearns</td>
<td>✓</td>
</tr>
<tr>
<td>JP Morgan Chase</td>
<td>✗</td>
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Next Steps

- Review with E&Y (as part of review of Netting Grid)

- Communicate again the Operating Rule around 80% minimum intra-month level

- Frequently review legal agreements and opinions to ensure appropriate documents are in place [eg, tri-party re-use agreements]