

Valuation & Control Report - Fixed Income Division

July 2008



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I

LBEX-WGM 790238

Executive summary

Complex Derivatives Transaction Review Committee

This committee, consisting of Capital Market Finance, Accounting Policy and Model Validation personnel, was set up in April 2005 and meets to consider any significant derivative transactions undertaken. The committee considers whether the transactions are being booked, valued and modeled appropriately. Furthermore, the committee determines whether the proper accounting treatment is being applied. During the month, the following transactions were reviewed:

- *Regulatory Capital Trades* – The desk has executed two new regulatory capital trades. Both trades mature on July 2023 with the clients having the option to call the trade on January 2009. For one of the trades, it was determined that even if 100% of the illiquid corporate loans defaulted by the call date, Lehman will not incur a loss if the average recovery rate is at least 12.3%. Historically, corporate loans have average recovery rate of at least 60-70%. For the other trade, it was determined that even if 85% of the illiquid Italian consumer loans defaulted by the call date with 0% recovery, Lehman will not incur a loss. Historically, Italian consumer loans have average default rate of 4-5% per annum. As such, Lehman's exposure to the illiquid corporate and Italian consumer loans are not deemed material economic risks, and thus, the trades meet the criteria for trading book designation. The trades have aggregate Day 1 P/L of \$50 million.
- *Equity Collar* – The SAP collar trade was previously discussed in September 2007 and January 2008. This trade was executed in May 2007 with Lehman essentially buying calls and selling puts on shares of SAP. The trade was partially amended as the maturity dates for some of the calls and puts were extended. Since the tenor of the trade was extended to seven years and implied volatilities beyond five years are deemed unobservable, the trade was transferred from level 2 to level 3 under FAS157. Furthermore, a funding adjustment was established to account for the client's ability to draw cash from Lehman up to an amount equal to the MTM in the client's favor. To reduce the net premium payment that the client will be paying Lehman, 25% of the trade was further restructured recently. A knock-out provision was added to this portion of the trade. Basically if the stock price of SAP falls below a specified threshold, this portion of the collar will be knocked-out. This latest restructuring generated a P/L of \$14.4 million. The current funding adjustment is \$6.5 million. The trade also has embedded liquidity, barrier shift and parameter uncertainty adjustments of \$71.8 million.
- *Equity Options* – Two related Turkish companies want to increase their stock liquidity. The two companies have granted to Lehman call and put options that expire in 9 months, 12 months and 15 months. Theoretically, Lehman will actively trade the stocks to delta hedge these options. Implied volatilities are deemed unobservable, and thus, the options will be classified as level 3 under FAS157. The desk will mark implied volatility at 60% of historical volatility. Stocks of the two companies have been posted as collateral for these option trades. Lehman is exposed to wrong-way counterparty risk on the put options. A counterparty valuation adjustment of \$1 million will be taken. This amount is derived by applying credit spread of 270 bps (based on loans issued by the two companies) on the full notional of the put options multiplied by two (to account for the difference in assumed recovery rates between loans and counterparty claims). The trade has Day 1 P/L of \$5 million.

Executive summary

Valuation adjustments (decreased by \$95mm from \$3,398mm to \$3,303mm, as detailed in section 2)

Significant changes include:

- Decrease of \$62mm of parameter uncertainty adjustments on recovery risk from CDO Europe is attributable to: 1) revised methodology that allows for the netting of systemic risk for issuers within the same region and 2) tightening of credit spreads particularly for monoline insurers.
- Decrease of \$28mm of prime representation and warranty adjustments from Securitized Product Americas to offset reimbursements to ALS for early payment defaults.
- Decrease of \$22mm of counterparty valuation adjustments from Commodity Americas is due to reduction of MTM of uncollateralized trades from lower gas and oil prices.
- Increase of \$26mm of counterparty valuation adjustments from Securitized Product Americas is attributable to: 1) increase in MTM on trades with monoline insurers and 2) increase in percentage of MTM needed to cover counterparty risk on trades with monoline insurers.

Price verification projects (further details in section 3)

In recent months, the Valuation and Control group:

- Initiated price testing of CMS spread options, CMS caps / floors, digital CMS options and inflation swaps / caps in Americas
- Increased FX skew testing coverage as well as initiated Totem submission of FX cross volatilities, FX FVA and FX barrier options in Americas
- Initiated price testing of heat rate options, distillates, and Eagle Energy Partners portfolio in Americas
- Enhanced price testing methodologies for ABS CDO and tranching ABX trades in Americas
- Initiated price testing of implied volatilities of fund derivative trades via cliquet options in Europe
- Increased commodity testing coverage including 60 newly traded curves in Europe
- Enhanced price testing methodology for credit options based on implied volatilities derived from Totem consensus prices in Europe
- Initiated Totem submission of housing indices as well as improved price testing methodologies for Securitized Product and Real Estate positions in Europe
- Initiated / expanded Totem submission of exotic rate products such as PRDC, FX TARN, CMS TARN, callable inverse floaters, callable CMS spreads, leveraged CMS spreads, inflation swaps and equity hybrid trades in Asia

The group is currently working on the following improvements:

- Enable full re-pricing of cap / floor skew positions with Totem results as well as establish price testing methodology for BMA swaptions and Bermudan options
- Continue to improve testing of mortgage derivatives and skew on mortgage options
- Establish deal review processes for exotic interest rate derivatives, fund derivatives and mortgage derivatives
- Expand Totem submission of FX exotics, such as baskets

Executive summary

Significant points on price verification (as detailed in section 3)

- Aggregate significant variance of \$1,921 million on the aggressive side, of which Americas has \$1,889 million, Europe has \$26 million and Asia has \$5 million.
- There are \$1,037 million of aggressive significant variances attributable to Securitized Product Americas. These variances are mainly from residual, whole loan, and prime legacy and subordinate RMBS positions; the desk has taken markdowns of \$300 million, \$446 million, and \$302 million respectively.
- There are \$705 million of aggressive significant variances attributable to Real Estate Americas. Real Estate positions are generally concentrated and/or illiquid. The desk has taken some markdowns in August and plans to take additional markdowns prior to quarter-end.
- There are \$126 million of aggressive significant variances attributable to Governments Americas. These variances are mainly from securities issued by government sponsored entities, which have experienced increased volatility and reduced liquidity. Desk disagrees with prices provided by external vendors but has agreed to take some markdowns where we have seen trades in the market and will monitor, in conjunction with PCG, for other items. All outstanding issues are to be resolved prior to quarter-end.

	Significant Pricing Variance - Global FID		
	in \$'000		
	<u>Re-marked</u>	<u>Resolved</u>	<u>Total</u>
Level 1	0	0	0
Level 2	(577,699)	(201,151)	(778,850)
Level 3	(539,732)	(169,700)	(709,432)
Derivatives	(4,654)	(30,677)	(35,332)
Consolidated Positions	(103,616)	(293,370)	(396,985)
Total	(1,225,701)	(694,898)	(1,920,599)

*Definition of pricing levels:

Level 1 : Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity has the ability to access at measurement date.

Level 2 : Inputs other than quoted prices included in Level 1 that are observable for the asset or liability either directly or indirectly. This includes quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active. Additionally inputs other than quoted prices that are observable for the asset or liability (eg interest rate and yield curves, observable at commonly quoted intervals, volatilities, prepayment speeds, loss severities, credit risks and default rates). Inputs that are derived principally from or corroborated by other means.

Level 3 : Unobservable inputs for the asset or liability.

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Valuation Adjustments

July 2008



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VALUATION ADJUSTMENTS – Significant changes

Region	Product	Description	Type	Current Month	Prior Month	Change	Comment
Americas	High Yield	Contingent Liability - LCDS Cancellation	Contingent Liabilities	12,332	0	12,332	Valuation adjustment is for potential cancellation of LCDS resulting in potential loss of MTM.
Americas	Commodities	Counterparty Valuation Adjustments	Credit	40,900	63,100	(22,200)	Lower gas and oil prices reduced the MTM of uncollateralized trades.
Americas	Commodities	Model - Quarterly Extendible	Model	11,100	0	11,100	New trade.
Americas	Securitized Products	Counterparty Valuation Adjustments	Credit	1,519,719	1,493,450	26,269	Increase is mainly attributable to: 1) increase in MTM on trades with monoline insurers and 2) increase in percentage of MTM needed to cover counterparty risk on trades with monoline insurers.
Americas	Securitized Products	Prime - Reps and Warranties	Contingent Liabilities	148,696	176,305	(27,609)	Valuation adjustment is reduced as Lehman reimburses ALS for early payment defaults.
Europe	IRP	Funding Cost	Valuation	28,269	39,596	(11,327)	Decline in interest rates during the month resulted in a decrease in MTM of inflation swaps with the Republic of Italy which reduced future funding cost.
Europe	CDO	Model Calibration	Model	(13,933)	4,955	(18,888)	Due to market volatility, model value from base correlation model is not reflective of market value. Valuation adjustment needed to properly reflect the implied correlation skews for CDX and LCDX. Valuation adjustment was reduced this month to true-up the value of non-super senior tranches.
Europe	CDO	Parameter Uncertainty	Liquidity	46,296	108,610	(62,314)	Decrease in parameter uncertainty adjustment on recovery risk is due to: 1) implementation of new methodology which bifurcates recovery risk between systemic risk (issuers with 5yr spread less than 1000 bps) and idiosyncratic risk (issuers with 5yr spread greater than 1000 bps) and allows the netting of systemic risk for issuers within the same region and 2) tightening of credit spreads particularly for monoline insurers.
Subtotal				1,793,379	1,886,016	(92,637)	
Remaining Valuation Adjustments				1,509,576	1,512,356	(2,781)	
Total Valuation Adjustments				3,302,955	3,398,372	(95,418)	

VALUATION ADJUSTMENTS – Summary

Business	Total \$000	Contingent							Early Termination	Valuation
		Model	Bid/Offer	Liabilities	Liquidity	Credit	Expense			
Liquid Market Prop	6,651	1,077	5,574	-	-	-	-	-	-	
Interest Rate Products	469,612	213,964	65,867	-	33,236	12,642	-	108,775	35,128	
Foreign Exchange	40,799	11,450	17,844	-	-	-	-	4,024	7,481	
High Grade Credit	60,546	1,533	45,928	3,448	3,840	1,469	1,328	3,000	-	
CDO	522,553	56,817	141,665	146,726	59,409	72,684	23,196	3,275	18,781	
High Yield	62,516	(2,886)	46,997	13,332	-	-	1,437	-	3,636	
Real Estate	1,640	-	1,594	-	-	-	46	-	-	
Munis	111,653	976	7,095	-	-	92,700	-	-	10,882	
Securitized Products	1,824,263	-	49,492	233,990	-	1,526,363	14,418	-	-	
Commodities Trading	174,937	40,101	64,971	-	2,565	40,900	-	-	26,400	
FID Corporate	27,784	524	21,161	-	1,440	-	-	4,659	-	
Total FID Valuation Adjustments	3,302,955	323,556	468,189	397,496	100,490	1,746,758	40,425	123,733	102,308	

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VALUATION ADJUSTMENTS – Regional matrix

America	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
Liquid Markets Prop	4,241	-	4,241	-	-	-	-	-	-
Interest Rate Products	122,248	94,505	10,998	-	10,225	6,520	-	-	-
Foreign Exchange	33,651	17,942	12,639	-	-	-	-	3,070	-
High Grade Credit	37,998	593	32,533	-	3,840	898	134	-	-
CDO	73,234	2,959	3,428	9,723	-	36,393	20,731	-	-
High Yield	50,833	(2,886)	40,387	13,332	-	-	-	-	-
Real Estate	1,594	-	1,594	-	-	-	-	-	-
Munis	111,653	976	7,095	-	-	92,700	-	-	10,882
Securitized Products	1,800,062	-	48,836	215,887	-	1,526,363	8,976	-	-
Commodities Trading	123,400	14,600	41,500	-	-	40,900	-	-	26,400
FID Corporate	6,205	-	6,205	-	-	-	-	-	-
Total America	2,365,120	128,689	209,457	238,942	14,065	1,703,774	29,841	3,070	37,282
Europe									
Capital Mkts Fund JV	111,506	8,401	7,018	-	-	-	-	96,087	-
Liquid Markets Prop	2,791	1,458	1,333	-	-	-	-	-	-
Interest Rate Products	186,416	96,472	30,372	-	17,493	1,122	-	12,688	28,269
Foreign Exchange	2,980	(10,355)	4,900	-	-	-	-	954	7,481
Commodities Trading	43,415	20,232	20,618	-	2,565	-	-	-	-
High Grade Credit	11,628	-	8,180	3,448	-	-	-	-	-
High Yield Credit	6,063	-	4,910	-	-	-	-	-	1,153
CDO	446,232	53,858	138,195	137,003	59,409	36,291	-	3,275	18,201
Securitized Products	18,759	-	656	18,103	-	-	-	-	-
FID Corporate	16,762	524	11,579	-	-	-	-	4,659	-
Total Europe	846,552	170,590	227,761	158,554	79,467	37,413	-	117,663	55,104
Asia									
Liquid Markets Prop	(381)	(381)	-	-	-	-	-	-	-
Interest Rate Products	49,442	14,586	17,479	-	5,518	5,000	-	-	6,859
High Grade Credit	10,920	940	5,215	-	-	571	1,194	3,000	-
CDO	3,087	-	42	-	-	-	2,465	-	580
Foreign Exchange	4,168	3,863	305	-	-	-	-	-	-
High Yield Credit	5,620	-	1,700	-	-	-	1,437	-	2,483
Real Estate	46	-	-	-	-	-	46	-	-
Securitized Products	5,442	-	-	-	-	-	5,442	-	-
Commodities Trading	8,122	5,269	2,853	-	-	-	-	-	-
FID Corporate	4,817	-	3,377	-	1,440	-	-	-	-
Total Asia	91,283	24,277	30,971	-	6,958	5,571	10,584	3,000	9,922
Global Total	3,302,955	323,556	468,189	397,496	100,490	1,746,758	40,425	123,733	102,308

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VALUATION ADJUSTMENTS – Americas

America - Valuation Adjs	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
LIQUID MARKETS PROP	4,241	0	4,241	0	0	0	0	0	0
Bid/Offer Adjustment	3,917		3,917						
FX Prop Bid/Offer Adjustment	324		324						
FID DERIVATIVES	122,248	94,505	10,998	0	10,225	6,520	0	0	0
Liquidity Adjustment	10,225				10,225				
Option Model Adjustment	30,453	30,453							
CVA	6,520					6,520			
Spread Bid/Offer	4,891		4,891						
Volatility Bid/Offer	6,107		6,107						
Deal Specific	64,052	64,052							
FOREIGN EXCHANGE	33,651	17,942	12,639	0	0	0	0	3,070	0
Bid/Offer	12,639		12,639						
FX Deal Specific - Model	6,480	6,480							
FX Deal Specific - Early Termination Adjustment	3,070							3,070	
Skew - Local Markets	2,745	2,745							
Skew - FX Options	8,717	8,717							
HIGH GRADE CREDIT	37,998	593	32,533	0	3,840	898	134	0	0
Bid/Offer Credit US	23,216		23,216						
Credit Adjustment - Enron	898					898			
Other Adjustments	61	39	22						
Bid Offer Latin	2,358		2,358						
Deal Specific Adjustments - Latin	2,469				2,335		134		
Other Adjustments - Latin	8,996	554	6,937		1,505				
CDOs	73,234	2,959	3,428	9,723	0	36,393	20,731	0	0
Expense Adjustment	20,731						20,731		
Contingent Liability	9,723			9,723					
Counterparty Valuation Adjustment	36,393					36,393			
Bid / Offer	3,428		3,428						
Model Adjustment	2,959	2,959							

VALUATION ADJUSTMENTS – Americas

America - Valuation Adjs	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
HIGH YIELD	50,833	(2,886)	40,387	13,332	0	0	0	0	0
Bid/Offer - SCT/Bonds/Distressed	29,249		29,249						
Contingent Liability - LCDS Cancellation	12,332			12,332					
Model	(2,886)	(2,886)							
Tax Indemnity Adjustment ANC (Fid Corp Loans)	1,000			1,000					
CDS Bid Offer (FID Corp Loans)	11,138		11,138						
REAL ESTATE	1,594	0	1,594	0	0	0	0	0	0
Bid / Offer - CMBX	1,594		1,594						
MUNIS	111,653	976	7,095	0	0	92,700	0	0	10,882
CDS Model Adjustment	696	696							
Counterparty Credit Adjustment	91,989					91,989			9,913
New Business Timing Items for deals not closed	9,913								
Derivatives Bid/Offer	7,095		7,095						
Libor Discounting / MMD Rate Lock valuation adj	280	280							
DSRF Put Valuation Adjustment	969								969
Cornell DSRF Credit Reserve	711					711			
SEURITIZED PRODUCTS	1,800,062	0	48,836	215,887	0	1,526,363	8,976	0	0
SCOR - Counterparty Credit Adjustment (trigger event)	2,500					2,500			
CAT - Beazley Deal Adjustment (trigger event)	1,885			1,885					
PFG - Contingent Liabilities/Referral Fees	2,123			2,123					
ABS - Bid / Offer Adjustment	32,542		32,542						
ABS - Counterparty Credit Adjustment	1,519,719					1,519,719			
Non Prime - Home Express (MGIC insurance)	17,042			17,042					
Non Prime - Reps and Warranties	27,125			27,125					
Non Prime - FHA/VA recourse risk	11,864			11,864					
Non Prime - Deal expenses/Due diligence	1,683						1,683		
Prime - Deal expenses/Due diligence	7,069						7,069		
Other - Deal expenses/Due diligence	224						224		
Non Resi - SBA Servicing Liabilities	6,573			6,573					
Loan loss adjustment	114			114					
Agency Remics/Strips - Non economic residuals	465			465					
Non Prime - Bid / Offer Adjustment	9,707		9,707						
Prime - Bid / Offer Adjustment	6,587		6,587						
Prime - Reps and Warranties	148,696			148,696					
PER Credit Adjustment	4,144					4,144			
COMMODITIES TRADING	123,400	14,600	41,500	0	0	40,900	0	0	26,400
Bid / Offer	41,500		41,500						
Deal Specific	26,400								26,400
Counterparty Credit Adjustment	40,900					40,900			
Model - Quarterly Extendible	11,100	11,100							
Model - Skew	3,500	3,500							
FID CORPORATE	6,205	0	6,205	0	0	0	0	0	0
CDO/SCT - Bid / Offer (range bounding)	6,205		6,205						
FID AMERICA TOTAL VALUATION ADJs	2,365,120	128,689	209,457	238,942	14,065	1,703,774	29,841	3,070	37,282

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VALUATION ADJUSTMENTS – Europe

Europe - Valuation Adjs	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
FID DERIVATIVES	186,416	96,472	30,372	0	17,493	1,122	0	12,688	28,269
Bid-offer : Correlation	23,201		23,201						
Bid-offer : Delta	5,262		5,262						
Bid-offer : Vega	1,909		1,909						
Contractual Early Termination Valuation Adjustment	12,688							12,688	
Counterparty Credit	1,122					1,122			
Funding Cost	28,269								28,269
Model : Approximation	10,103	10,103							
Model : Barrier shift	11,801	11,801							
Model : Calibration	2,208	2,208							
Model : Fit	27,546	27,546							
Model : Skew	30,584	30,584							
Model : Unapproved model	14,230	14,230							
Parameter Uncertainty	17,493				17,493				
COMMODITIES TRADING	43,415	20,232	20,618	0	2,565	0	0	0	0
Parameter Uncertainty	2,565				2,565				
Bid-offer : Correlation	4,024		4,024						
Bid-offer : Delta	15,281		15,281						
Bid-offer : Vega	1,313		1,313						
Model : Skew	3,964	3,964							
Model : Unapproved model	16,268	16,268							
CAPITAL MARKETS FUND DERIVATIVES JV	111,506	8,401	7,018	0	0	0	0	96,087	0
Bid-offer : Vega	7,018		7,018						
Contractual Early Termination Valuation Adjustment	96,087							96,087	
Model : Skew	8,401	8,401							
CDO	446,232	53,858	138,195	137,003	59,409	36,291	0	3,275	18,201
Bid-offer : Delta	137,265		137,265						
Bid-offer : Vega	930		930						
Contingent Deal	21,927			21,927					
Contingent Liability	115,076			115,076					
Counterparty Valuation Adjustment	36,291					36,291			
Funding Cost	2,034								2,034
Model : Approximation	28,955	28,955							
Contractual Early Termination Valuation Adjustment	437							437	
Model : Calibration	(13,933)	(13,933)							
Model : Fit	37,996	37,996							
Model : Skew	840	840							
Non-Contractual Early Termination Valuation Adjustment	2,838							2,838	
Parameter Uncertainty	46,296				46,296				
P&L pending deal review	16,167								16,167
Liquidity - Concentration	13,113				13,113				

VALUATION ADJUSTMENTS – Europe

Europe - Valuation Adjs	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
HIGH GRADE CREDIT	11,628	0	8,180	-3,448	0	0	0	0	0
Bid-offer : Delta	8,180		8,180						
Contingent Liability	3,448			3,448					
HIGH YIELD CREDIT	6,063	0	4,910	0	0	0	0	0	1,153
Bid-offer : Delta	2,349		2,349						
Deal Specific - To be re-categorised	418								418
Bid-offer : Delta (FID Corp Loans)	1,382		1,382						
Bid-offer : Delta (High Yield EEMEA)	1,179		1,179						
Deal Specific - To be re-categorised (High Yield EEMEA)	735								735
LIQUID MARKETS PROP	2,791	1,458	1,333	0	0	0	0	0	0
Bid-offer : Delta	1,333		1,333						
Model : Skew	1,458	1,458							
FX	2,980	(10,355)	4,900	0	0	0	0	954	7,481
Bid-offer : Vega	4,900		4,900						
Model : Skew	(10,355)	(10,355)							
Non-Contractual Early Termination Valuation Adjustment	954							954	
Deal Specific - To be re-categorised (FX EEMEA)	7,481								7,481
SEURITIZED PRODUCTS	18,759	0	656	18,103	0	0	0	0	0
Contingent Liability	18,103			18,103					
Bid-offer : Delta	656		656						
FID Corporate	16,762	524	11,579	0	0	0	0	4,659	0
Bid-offer	11,579		11,579						
Contractual Early Termination Valuation Adjustment	4,659							4,659	
Model : Skew	524	524							
FID EUROPE TOTAL VALUATION ADJS	846,552	170,590	227,761	158,554	79,467	37,413	0	117,663	55,104

VALUATION ADJUSTMENTS – Asia

Asia - Valuation Adjs	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
LIQUID MARKETS PROP	(381)	(381)	0	0	0	0	0	0	0
Model	(381)	(381)							
FID DERIVATIVES	49,442	14,586	17,479	0	5,518	5,000	0	0	6,859
Bid/Offer	17,479		17,479						
Model Adjustment	14,586	14,586							
Liquidity Adjustment	5,518				5,518				
Credit Adjustment	5,000					5,000			
CMT Proxy Marking Adjustment	4,282								4,282
Exotics Price Testing Adjustment	2,577								2,577
HIGH GRADE CREDIT	10,920	940	5,215	0	0	571	1,194	3,000	0
Documentation adjustments	687						687		
Bid/Offer	5,214		5,214						
Corr and Vol - CMDS	940	940							
Early Termination Adjustment	3,000							3,000	
Adjustment against claim for Enron	400					400			
Deal Specific	679		1			171	507		
CDO	3,087	0	42	0	0	0	2,465	0	580
Deal Specific	580								580
Documentation and legal fee adjustments	2,465						2,465		
Bid/Offer Adjustments	42		42						
FX	4,168	3,863	305	0	0	0	0	0	0
Bid / Offer Adjustment	305		305						
Model Adjustment	3,863	3,863							

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VALUATION ADJUSTMENTS – Asia

Asia - Valuation Adjs	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
HIGH YIELD	5,620	0	1,700	0	0	0	1,437	0	2,483
Expense Adjustments	1,437						1,437		
Bid/Offer Adjustment	1,700		1,700						
Deal Specific Adjustment	2,483								2,483
REAL ESTATE	46	0	0	0	0	0	46	0	0
Expense Adjustment	46						46		
SECURITIZED PRODUCTS	5,442	0	0	0	0	0	5,442	0	0
Expense Adjustment	3,329						3,329		
Adjustment for Receivable of GFFS's Buyer and Legal Expenses	2,113						2,113		
Commodities Trading	8,122	5,269	2,853	0	0	0	0	0	0
Bid / Offer Adjustment	2,853		2,853						
Model Adjustment	5,269	5,269							
FID CORP	4,817	0	3,377	0	1,440	0	0	0	0
Bid / Offer	41		41						
Liquidity	1,440				1,440				
Range-bounding Adjustment	3,336		3,336						
FID ASIA TOTAL VALUATION ADJS	91,283	24,277	30,971	0	6,958	5,571	10,584	3,000	9,922

VALUATION ADJUSTMENTS – Monthly changes

Business	Total	Model	Contingent				Early		Valuation
			Bid/Offer	Liabilities	Liquidity	Credit	Expense	Termination	
Liquid Market Prop	(643)	398	(1,041)	-	-	-	-	-	-
Interest Rate Products	(14,491)	3,883	(5,606)	-	(482)	654	-	(1,388)	(11,552)
Foreign Exchange	3,738	4,655	(731)	-	-	-	-	(115)	(71)
High Grade Credit	3,573	39	545	-	-	-	(11)	3,000	-
CDO	(75,626)	(15,640)	(1,003)	795	(62,320)	(887)	(857)	(716)	5,002
High Yield	9,959	(1,086)	(1,869)	12,332	-	-	(70)	-	652
Real Estate	1,594	-	1,594	-	-	-	-	-	-
Munis	(3,569)	(45)	(502)	-	-	(7,401)	-	-	4,379
Securitized Products	(18,462)	-	(3,559)	(39,907)	(742)	26,055	(309)	-	-
Commodities Trading	(1,198)	16,645	1,793	-	(436)	(22,200)	-	-	3,000
FID Corporate	(293)	-	(236)	-	-	-	-	(57)	-
Total FID Adjustments	(95,418)	8,849	(10,615)	(26,780)	(63,980)	(3,779)	(1,247)	724	1,410

VALUATION ADJUSTMENTS – Monthly changes

America	Total	Model	Bid/Offer	Contingent Liabilities	Liquidity	Credit	Expense	Early Termination	Valuation
Liquid Markets Prop	(1,041)	-	(1,041)	-	-	-	-	-	-
Interest Rate Products	9,571	9,970	(1,116)	-	685	32	-	-	-
Foreign Exchange	(2,878)	(2,854)	(376)	-	-	-	-	352	-
High Grade Credit	279	39	240	-	-	-	-	-	-
CDO	(5,492)	(5,603)	(309)	-	-	823	(403)	-	-
High Yield Credit	10,111	(1,086)	(1,135)	12,332	-	-	-	-	-
Real Estate	1,594	-	1,594	-	-	-	-	-	-
Munis	(3,569)	(45)	(502)	-	-	(7,401)	-	-	4,379
Securitized Products	(12,614)	-	(500)	(37,987)	-	26,055	(182)	-	-
Commodities Trading	(4,600)	14,600	-	-	-	(22,200)	-	-	3,000
FID Corporate	-	-	-	-	-	-	-	-	-
Total America	(8,639)	15,021	(3,145)	(25,655)	685	(2,691)	(585)	352	7,379
Europe									
Capital Mkts Fund JV	(246)	(110)	1,182	-	-	-	-	(1,318)	-
Liquid Markets Prop	398	398	-	-	-	-	-	-	-
Interest Rate Products	(22,134)	(5,937)	(5,301)	-	104	622	-	(70)	(11,552)
Foreign Exchange	5,731	6,268	1	-	-	-	-	(467)	(71)
Commodities Trading	1,118	645	909	-	(436)	-	-	-	-
High Grade Credit	(308)	-	(308)	-	-	-	-	-	-
High Yield Credit	(717)	-	(711)	-	-	-	-	-	(6)
CDO	(70,134)	(10,037)	(694)	795	(62,320)	(1,710)	-	(716)	4,548
Securitized Products	(5,721)	-	(3,059)	(1,920)	(742)	-	-	-	-
FID Corporate	(293)	-	(236)	-	-	-	-	(57)	-
Total Europe	(92,306)	(8,773)	(8,217)	(1,125)	(63,394)	(1,088)	-	(2,628)	(7,081)
Asia									
Liquid Markets Prop	-	-	-	-	-	-	-	-	-
Interest Rate Products	(1,682)	(40)	(371)	-	(1,271)	-	-	-	-
High Grade Credit	3,602	-	613	-	-	-	(11)	3,000	-
CDO	-	-	-	-	-	-	(454)	-	454
Foreign Exchange	885	1,241	(356)	-	-	-	-	-	-
High Yield Credit	565	-	(23)	-	-	-	(70)	-	658
Real Estate	-	-	-	-	-	-	-	-	-
Securitized Products	(127)	-	-	-	-	-	(127)	-	-
Commodities Trading	2,284	1,400	884	-	-	-	-	-	-
FID Corporate	-	-	-	-	-	-	-	-	-
Total Asia	5,527	2,601	747	-	(1,271)	-	(662)	3,000	1,112
Global Total	(95,418)	8,849	(10,615)	(26,780)	(63,980)	(3,779)	(1,247)	724	1,410

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III

Pricing Report
July 2008



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PRICING REPORT – Explanation of significant variances

Business	Exposure Type	Level	Risk Measure	Exposure Size \$'000	Initial Variance \$'000	Remarkd \$'000	Resolved \$'000	Resolution
<i>Americas</i>								
IRP - Derivatives	Agency CMO Bonds	2	MV	292,689	7,211		7,211	PCG is currently reviewing the existing price testing methodology with the desk.
IRP - Derivatives	TBA Hedges	2	MV	4,522,814	7,076		7,076	Variance is due to size of position held. Actual variance is 0.2%.
IRP - Derivatives	Constant Maturity Mortgage Swap	2	PV01	8,007	4,249		4,249	PCG is currently reviewing the existing price testing methodology with the desk.
IRP - Governments	Government Sponsored Enterprises (Fannie Mae, Freddie Mac, FHLB, Federal Farm Credit Bank)	2	MV	342,860	(74,577)		(74,577)	PCG has discussed this variance with the desk. Desk disagrees with external price but has agreed to take some mark downs.
IRP - Governments	TVA	2	MV	1,394,902	(37,440)		(37,440)	PCG has discussed this variance with the desk. Desk disagrees with external price. Market is extremely illiquid. PCG is currently discussing with external vendor about their methodology and with the desk about taking a liquidity adjustment.
IRP - Governments	Egypt Government Bond	2	MV	464,828	(13,587)		(13,587)	PCG substantiated desk mark with trading activity.
High Grade	TC GROUP INVESTMENT HOLDINGS	2	MV	107,719	(3,211)		(3,211)	Variance is due to size of position held. Actual variance is 3.0%.
High Grade	STAPLES BRIDGE 04-01-08/REVOLVER	2	MV	415,382	(2,299)		(2,299)	Variance is due to size of position held. Actual variance is 0.6%.
High Grade	STAPLES BRIDGE 04-01-08/REVOLVER	2	MV	348,921	(1,931)		(1,931)	Variance is due to size of position held. Actual variance is 0.6%.
High Grade	ALTRIA GROUP 364-DAY BRIDGE	2	MV	897,750	1,732		1,732	Variance is due to size of position held. Actual variance is 0.2%.
High Grade	CLP HOLDINGS LLC (1/2/08)/TERM	2	MV	210,906	1,594		1,594	Variance is due to size of position held. Actual variance is 0.8%.
High Grade	ALCOA INC. (1/31/08)/REVOLVER	2	MV	497,500	752		752	Variance is due to size of position held. Actual variance is 0.2%.
High Grade	WHITE MOUNTAINS (6/19/07)/5-YR	2	MV	28,031	639		639	Variance is due to size of position held. Actual variance is 2.3%.
High Grade	XL CAP LTD PREF ORD SHS R/M	2	MV	3,959	(518)		(518)	Re-tested in August and variance was within threshold.
High Grade	TRANSOCEAN 2 YR TERM LOAN	2	MV	54,533	504		504	Variance is due to size of position held. Actual variance is 0.9%.
High Grade	S	2	CS01	(9)	(1,357)		(1,357)	Re-tested in August and variance was within threshold.
High Grade	IACI	2	CS01	9	(1,191)		(1,191)	Variance is attributable to no-restructuring curve. Desk mark is within acceptable standard deviations away from Markit mean. PCG also substantiated desk mark with trading activities of modified-restructuring curve.
High Grade	CIT	2	CS01	(4)	(1,181)		(1,181)	Variance is attributable to no-restructuring curve. Desk mark is within acceptable standard deviations away from Markit mean. PCG also substantiated desk mark with trading activities of modified-restructuring curve.
High Grade	LIZ	2	CS01	7	(980)		(980)	Desk mark is within bid/offer.
High Grade	KBH	2	CS01	4	(979)	(979)		Remarkd.
High Grade	CTL	2	CS01	(73)	(765)		(765)	Desk mark is within acceptable standard deviations away from Markit mean.
High Grade	MS	2	CS01	(9)	754	754		Remarkd.
High Grade	JNY	2	CS01	(14)	(646)		(646)	Variance is attributable to no-restructuring curve. PCG substantiated desk mark by benchmarking to modified-restructuring curve.
High Grade	TOL	2	CS01	2	(641)		(641)	Variance is attributable to no-restructuring curve. Desk mark is within acceptable standard deviations away from Markit mean. PCG also substantiated desk mark with trading activities of modified-restructuring curve.
High Grade	CDX_IG_1210	2	IND001	(263)	772		772	Variance is due to size of position held. Actual variance is 2.9 bps.

PRICING REPORT – Explanation of significant variances

Business	Exposure Type	Level	Risk Measure	Exposure Size \$ '000	Initial Variance \$'000	Marked \$ '000	Resolved \$ '000	Resolution
High Yield	HMH PUBLISHING MEZZANINE(PIK)	2	MV	122,164	2,681		2,681	Variance is due to size of position held. Actual variance is 2.2%.
High Yield	HMH PUBLISHING MEZZANINE(PIK)	2	MV	108,000	2,370		2,370	Variance is due to size of position held. Actual variance is 2.2%.
High Yield	HMH PUBLISHING MEZZANINE(PIK)	2	MV	66,350	1,456		1,456	Variance is due to size of position held. Actual variance is 2.2%.
High Yield	HMH PUBLISHING FIRST LIEN	2	MV	129,000	1,134		1,134	Variance is due to size of position held. Actual variance is 0.9%.
High Yield	DHS DRILLING COMPANY/TERM LOAN	2	MV	74,250	1,468		1,468	Variance is due to size of position held. Actual variance is 2.0%.
High Yield	FAIRPOINT COMMUNICATIONS	2	MV	60,164	(1,414)		(1,414)	Variance is due to size of position held. Actual variance is 2.4%.
High Yield	FAIRPOINT COMMUNICATIONS	2	MV	32,256	1,002		1,002	Variance is due to size of position held. Actual variance is 3.1%.
High Yield	ARINC 1ST LIEN(10/25/07)/FIRST LIEN	2	MV	91,014	1,112		1,112	Variance is due to size of position held. Actual variance is 1.2%.
High Yield	ARINC 1ST LIEN(10/25/07)/REVOLVER	2	MV	42,500	920		920	Variance is due to size of position held. Actual variance is 2.2%.
High Yield	US INVESTIGATION SERVICES	2	MV	50,895	973		973	Variance is due to size of position held. Actual variance is 1.9%.
High Yield	HTN	2	CS01	(43)	(7,897)		(7,897)	Trader provided support to substantiate its mark by referencing to Riverdeep first lien loan CDS (HTN was recently acquired by Riverdeep) since HTN bonds (deliverable for HTN CDS) are pari-passu with Riverdeep first lien loans.
High Yield	SBG1	2	CS01	(26)	(3,540)		(3,540)	PCG substantiated desk mark with trading activities.
High Yield	MGM	2	CS01	(4)	(3,423)		(3,423)	Variance is attributable to subordinate curve which is marked relative to the senior curve.
High Yield	HCA	2	CS01	37	(2,390)		(2,390)	PCG substantiated desk mark with trading activities.
High Yield	THC	2	CS01	(1)	(2,027)		(2,027)	Tenet Healthcare is trading at wide bid/offer spread. PCG has proposed additional bid/offer adjustments due to current market environment.
High Yield	URI	2	CS01	(31)	(1,971)		(1,971)	United Rentals is trading at wide bid/offer spread. PCG has proposed additional bid/offer adjustments due to current market environment.
High Yield	KBH	2	CS01	(12)	(1,884)		(1,884)	Position is marked by the HG desk with the HY desk being a price taker.
High Yield	CDX_HY_BB_S7_1211_X1	2	IND001	135	(3,423)		(3,423)	PCG substantiated desk mark with trading activities.
High Yield	CDX_HY_B_S6_0611	2	IND001	(115)	(2,397)		(2,397)	Index is off-the-run and illiquid. Actual variance is 20.8 bps.
High Yield	CDX_HY_100_S9_1210_X1	2	IND001	(453)	(2,014)		(2,014)	Variance is due to size of position held. Actual variance is 4.4 bps.
Bank Loans	GENERAL ELECT CAPITAL CORP	2	MV	615,625	(7,217)		(7,217)	Variance is due to size of position held. Actual variance is 1.2%.
Bank Loans	GENERAL ELECT CAPITAL CORP	2	MV	246,250	(2,887)		(2,887)	Variance is due to size of position held. Actual variance is 1.2%.
Bank Loans	GECC 1 YEAR/1 YEAR REVOLVER	2	MV	331,335	(3,498)		(3,498)	Variance is due to size of position held. Actual variance is 1.1%.
Bank Loans	BEST BUY CO (9/19/07)/5YR	2	MV	173,700	(4,334)		(4,334)	Variance is due to size of position held. Actual variance is 2.5%.
Bank Loans	FORD MOTOR COMPANY (12/15/06)	2	MV	469,700	4,270		4,270	Variance is due to size of position held. Actual variance is 0.9%.

PRICING REPORT – Explanation of significant variances

Business	Exposure Type	Level	Risk Measure	Exposure Size \$'000	Initial Variance \$'000	Remarkd \$'000	Resolved \$'000	Reotation
Bank Loans	BLACKROCK INC. (8/22/07)/REVOLVER	2	MV	137,970	(4,148)		(4,148)	Variance is due to size of position held. Actual variance is 3.0%.
Bank Loans	SEARS HOLDINGS CORP. (3/24/05)	2	MV	181,213	(3,755)		(3,755)	Variance is due to size of position held. Actual variance is 2.1%.
Bank Loans	TXU ENERGY (10/10/07) CITI/REVOLVER	2	MV	272,311	3,142		3,142	Variance is due to size of position held. Actual variance is 1.2%.
Bank Loans	METLIFE 3BN (6-20-07)/5-YEAR	2	MV	147,600	2,711		2,711	Variance is due to size of position held. Actual variance is 1.8%.
Bank Loans	SLM CORP 5 YR 2BN 10/20/06	2	MV	88,358	1,959		1,959	Variance is due to size of position held. Actual variance is 2.2%.
Bank Loans	SLM CORP 5YR 2BN 10/20/05	2	MV	91,750	1,923		1,923	Variance is due to size of position held. Actual variance is 2.1%.
Cash CDO	GSC INV (CDO)	2	MV	16,896	(569)		(569)	Variance is due to size of position held. Actual variance is 3.4%.
Cash CDO	ARES CLO	2	MV	19,764	(502)		(502)	Variance is due to size of position held. Actual variance is 2.5%.
Cash CDO	CDX_IG_1211	2	IND001	(546)	(758)		(758)	Variance is due to size of position held. Actual variance is 1.4 bp.
Emerging Market	VENZ	2	CS01	(96)	(2,090)		(2,090)	Desk provided external support to substantiate mark.
Emerging Market	ARGENT	2	CS01	(146)	(816)		(816)	PCG was able to substantiate desk mark with Markit data.
Emerging Market	PHILIP	2	CS01	(6)	(508)		(508)	Variance is attributable to the 8Y point which is interpolated. PCG discussed variance with the desk and they provided explanation of their interpolation methodology.
Muni - Cash	HILLSBOROUGH CNTY FLA AVIATION	2	MV	1,339	(1,071)		(1,071)	Delta Airline bonds. The \$5mm notional Hillsborough County position is part of the total outstanding of \$8mm bonds related to a maintenance facility which the lease has already been rejected by the courts. This is a work-out situation and the desk has negotiated a settlement with Delta that is consistent with the current mark.
Muni - Cash	PUERTO RICO COMWLTH HWY & TRAN	2	MV	20,700	(845)	(845)		Remarkd.
Muni - Cash	PUERTO RICO COMWLTH INFRASTRUC	2	MV	24,600	1,295		1,295	There has been no recent trading activity. PCG is comfortable with conservative mark since position is illiquid.
Muni - Cash	El Paso Single Family Housing (AMT)	2	MV	10,711	(819)		(819)	Bonds are priced to average life and IDC is pricing to maturity, and thus, ignoring the quicker prepayment of this structure. Desk also disagrees with IDC's valuations on similar bonds. The desk is in discussion with IDC to explain how these bonds should be valued. PCG has observed improvements in the variances of housing bonds.
Muni - Cash	Texas Single Family Housing (AMT)	2	MV	16,765	(527)		(527)	Bonds are priced to average life and IDC is pricing to maturity, and thus, ignoring the quicker prepayment of this structure. Desk also disagrees with IDC's valuations on similar bonds. The desk is in discussion with IDC to explain how these bonds should be valued. PCG has observed improvements in the variances of housing bonds.
Muni - Cash	CALIFORNIA ST (AMT)	2	MV	39,378	(758)		(758)	PCG substantiated desk mark with trading activities.
Muni - Cash	CALIFORNIA HSG FIN AGY REV (AMT)	2	MV	13,580	(1,002)		(1,002)	Bonds are priced to average life and IDC is pricing to maturity, and thus, ignoring the quicker prepayment of this structure. Desk also disagrees with IDC's valuations on similar bonds. The desk is in discussion with IDC to explain how these bonds should be valued. PCG has observed improvements in the variances of housing bonds.
Muni - Cash	CALIFORNIA STATEWIDE CMNTYS DE	2	MV	13,800	506		506	This is an illiquid FRN position and desk has marked conservatively to external price.
Muni - Cash	CALIFORNIA STATEWIDE CMNTYS DE	2	MV	28,980	1,063		1,063	This is an illiquid FRN position and desk has marked conservatively to external price.
Muni - Cash	OAKLAND CNTY MICH CTFS PARTN M	2	MV	33,354	520		520	Variance is due to size of position held. Actual variance is 1.6%.

PRICING REPORT – Explanation of significant variances

Business	Exposure Type	Level	Risk Measure	Exposure Size \$'000	Initial Variance \$'000	Revised \$'000	Resolved \$'000	Resolution
Muni - Cash	NEW YORK CITY N Y INDL DEV AGY	2	MV	38,120	1,045		1,045	Variance is due to size of position held. Actual variance is 2.7%.
Muni - Cash	NEW YORK CITY N Y INDL DEV AGY	2	MV	60,911	1,235		1,235	Variance is due to size of position held. Actual variance is 2.0%.
Muni - Cash	NEW YORK CITY N Y INDL DEV AGY	2	MV	97,121	2,237		2,237	Variance is due to size of position held. Actual variance is 2.3%.
Muni - Cash	MINNEAPOLIS ST PAUL MINN HSG (AMT)	2	MV	37,831	2,720		2,720	Bonds are priced to average life and IDC is pricing to maturity, and thus, ignoring the quicker prepayment of this structure. Desk also disagrees with IDC's valuations on similar bonds. The desk is in discussion with IDC to explain how these bonds should be valued. PCG has observed improvements in the variances of housing bonds.
Securitized Product	Residuals	3	MV	705,175	(250,607)	(250,607)		Desk has taken mark downs of \$300 million.
Securitized Product	Whole Loans	2	MV	3,981,839	(211,141)	(211,141)		Desk has taken mark downs of \$245 million.
Securitized Product	Whole Loans	3	MV	1,573,520	(152,252)	(152,252)		Desk has taken mark downs of \$201 million.
Securitized Product	CEAGO 2007-1A A1 CEAGO ABD CDO	3	MV	417,016	(38,834)		(38,834)	ABS CDO market has been extremely illiquid and volatile. PCG derived price based on value of underlying securities. Position was hedged by purchasing CDS protection from XLCA. Positive variance from the CDS has been netted with negative variance from cash position to generate net negative variance balance. PCG discussed variance with the desk and concluded that variance is reasonable given current market conditions.
Securitized Product	Prime MBS	2	MV	543,857	(319,583)	(319,583)		Variance is attributable to prime legacy and subordinate positions. Desk has taken mark downs of \$236 million.
Securitized Product	Prime MBS	3	MV	78,444	(65,411)	(65,411)		Variance is attributable to prime legacy and subordinate positions. Desk has taken mark downs of \$66 million.
Real Estate	237 Park Bridge Mezz	2	MV	281,389	(46,531)	(46,531)		Desk has taken a mark down of \$45 million.
Real Estate	LB West Bay Development LLC	C	MV	76,488	(39,224)	(39,224)		Desk has taken a mark down of \$25 million.
Real Estate	Grand Prix	2	MV	346,949	(36,235)		(36,235)	As of July 08, there is a bid by GE on \$247mm senior position at price of 88 or dealer mark of approximately 561 bps. Using this information, it is reasonable to use price of 80 or dealer mark of 829 bps on the remaining mezz position. Currently under discussion with desk.
Real Estate	Prestige Portfolio	3	MV	56,625	(27,670)	(27,670)		Desk has taken a mark down of \$15 million.
Real Estate	Monument Realty Line	C	MV	36,395	(23,419)	(23,419)		Desk has taken a mark down of \$23 million.
Real Estate	Greenwich Place Acquisition LLC	C	MV	119,516	(21,156)		(21,156)	Greenwich Place, is a 266-unit multi-family development located in Greenwich, Connecticut. Units under renovation. Strong leasing activity. Signed 13 leases in past 2 months. Currently under discussion with desk.
Real Estate	Petrini Bakersfield	C	MV	34,341	(20,296)		(20,296)	Petrini Bakersfield is 1810 acres of land located in Southwest Bakersfield, CA. The business plan is to entitle and bulk sale 6,087 lots in paper and finished lot condition. Recent offers have fallen out of contract. A letter of default has been sent out due to missed interest payment and foreclosure will be pursued. Currently under discussion with desk.
Real Estate	Montelucia Hotel & Villas Mezz	3	MV	30,550	(20,000)	(20,000)		Desk has taken a mark down of \$20 million.
Real Estate	Greenwich Oaks Acquisition LLC	C	MV	82,834	(19,440)		(19,440)	Greenwich Oaks, is a 130-unit multi-family development located in Greenwich, Connecticut with 38% occupancy. Leasing effort will begin early 2009. Exterior is 95% completed and the remaining 5% is mostly gutter and minor patch work. Currently under discussion with desk.
Real Estate	Swenson Construction LLC	C	MV	56,163	(17,966)	(17,966)		Desk has taken a mark down of \$10 million.
Real Estate	LB Bell Road (Nashville) Portfolio	C	MV	13,601	(13,601)		(13,601)	Consists of 5 multi-family properties containing 1,593 units located in Tennessee. Current occupancy is 85.81%. Units are turning over. Currently under discussion with desk.
Real Estate	Indiantown	3	MV	17,852	(12,485)		(12,485)	Indiantown is a 2,250 lot residential development site in Indiantown, Martin County, Florida. The final DRI, Development Order, Rezoning, and Master Site Plan approval for 2,250 residential units and 150,000 sq ft of commercial space to be built on the property is currently on hold. Business plan is being re-evaluated. Currently under discussion with desk.

PRICING REPORT – Explanation of significant variances

Business	Exposure Type	Level	Risk Measure	Exposure Size \$'000	Initial Variance \$'000	Remarkd \$'000	Resolved \$'000	Resolution
Real Estate	North Peak	C	MV	18,584	(12,398)		(12,398)	The property is a partially entitled 1,200 home site community in the city of Lake Elsinore, Riverside County, CA. Lehman foreclosed on the property and currently in the process of disposing the asset through auction sale. Currently under discussion with desk.
Real Estate	PCCP-Roseville (PAMI direct)	3	MV	11,980	(11,980)	(11,980)		Desk has taken a mark down of \$7.5 million.
Real Estate	LB NWP LLC	C	MV	11,970	(11,970)	(11,970)		Desk has taken a mark down of \$6 million.
Real Estate	Boulder Springs	3	MV	41,895	(11,812)	(11,812)		Desk has taken a mark down of \$12 million.
Real Estate	LB Ridge Crossing LLC	C	MV	28,329	(11,319)		(11,319)	Ridge Crossing Apartments is located in Hoover submarket of Birmingham in Jefferson County, AL. The property is a garden style apartment complex and is a class A product. The property's total net rentable area is 797,492 sf, which is situated on 86 acres. Occupancy for April 2008 was 94%. Renovations have been completed on two units and one of them was released at a significant rent increase. In discussion with the business.
Real Estate	LB South Beach LLC	C	MV	75,566	(11,036)	(11,036)		Desk has taken a mark down of \$7 million.
Real Estate	Whitworth Estates Senior	3	MV	20,959	(10,674)		(10,674)	Whitworth Estates is 154 acres of raw land located in Florida, which is fully entitled as a PUD under Palm Beach County zoning, allowing for 380 single family home sites. The business plan is to hold the property for two years while the surrounding area is built out and the housing market stabilizes. Lehman is currently in negotiations with the borrower for a Deed in Lieu transaction. In discussion with the business.
Real Estate	Lake Merritt	C	MV	10,284	(10,284)		(10,284)	The development consists of 237 for-sale residential luxury condominiums located in Oakland, CA. The predevelopment portion of the project is completed. The borrower has admitted to being "out of the money" on this deal and has offered to "give back" the property to the lender. Senior debt matured on 11/30/07 and Lehman bought the senior debt with 90% seller financing. LB will be pursuing foreclosure on the mezz loans. In discussion with the business.
Real Estate	Miscellaneous	2	MV	N/A	(22,584)		(22,584)	Other significant variances
Real Estate	Miscellaneous	3	MV	N/A	(107,708)		(107,708)	Other significant variances
Real Estate	Miscellaneous	C	MV	N/A	(184,877)		(184,877)	Other significant variances
					(1,889,252)	(1,221,672)	(667,580)	
Europe								
Firm Relationship Loans	Teleco Italia	2	MV	197,582	1,847		1,847	Variance is due to size of position held. Actual variance is 0.9%
Firm Relationship Loans	Mubadala	2	MV	95,238	1,471		1,471	PCG price is based on proxy CDS spread. Actual variance is 1.5%.
Firm Relationship Loans	NIBC	2	MV	155,577	1,352		1,352	Variance is due to size of position held. Actual variance is 0.9%
Firm Relationship Loans	Vodafone	2	MV	200,000	1,053		1,053	Variance is due to size of position held. Actual variance is 0.5%
Firm Relationship Loans	Deutsche Telecom	2	MV	933,461	(983)		(983)	Variance is due to size of position held. Actual variance is 0.1%
High Yield	ProSiebenSat.1 loan	2	MV	89,627	(2,996)	(2,996)		Remarkd.
High Yield	Merlin Loan	2	MV	154,450	(1,203)		(1,203)	Business had initial aggressive variance of \$7 million and subsequently taken mark downs of \$5 million. Remaining variance of \$2 million is deemed acceptable.
High Yield	Gala	2	MV	27,165	(1,030)		(1,030)	Business had initial aggressive variance of \$7 million and subsequently taken mark downs of \$5 million. Remaining variance of \$2 million is deemed acceptable.

PRICING REPORT – Explanation of significant variances

Business	Exposure Type	Level	Risk Measure	Exposure Size \$'000	Initial Variance \$'000	Marked \$'000	Resolved \$'000	Resolution
High Yield	Kion	2	MV	19,023	(801)		(801)	Business had initial aggressive variance of \$7 million and subsequently taken mark downs of \$5 million. Remaining variance of \$2 million is deemed acceptable.
High Yield	YPSO	2	MV	29,343	734		734	Business had initial aggressive variance of \$7 million and subsequently taken mark downs of \$5 million. Remaining variance of \$2 million is deemed acceptable.
High Yield	Klockner Pentaplast	2	MV	53,200	584	584		Marked.
High Yield	CWT	2	MV	25,000	(532)		(532)	Business had initial aggressive variance of \$7 million and subsequently taken mark downs of \$5 million. Remaining variance of \$2 million is deemed acceptable.
High Yield	Dako	2	MV	37,513	658	658		Marked.
High Yield	Borsodchem	2	MV	35,264	2,380	2,380		Marked.
Bespoke Correlation	C	D	CS01	(10)	(1,696)		(1,696)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	MER	D	CS01	(39)	(1,573)		(1,573)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	IAR	D	CS01	(2)	(1,170)		(1,170)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	CS01 AIFUL	D	CS01	(3)	(1,082)		(1,082)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	BZH.USD.SENIOR_NORE.DERIV	D	REC01	188	(6,511)		(6,511)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	FGIC.USD.SENIOR_MODRE.DERIV	D	REC01	531	(4,550)		(4,550)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	LEN.USD.SENIOR_MODRE.DERIV	D	REC01	149	(4,460)		(4,460)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	GLBIR.USD.SENIOR_MMR_L.DERIV	D	REC01	242	(2,740)		(2,740)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	FGIC.EUR.SENIOR_MODRE.DERIV	D	REC01	238	(2,037)		(2,037)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
Bespoke Correlation	HOV.USD.SENIOR_NORE.DERIV	D	REC01	188	(1,877)		(1,877)	Business has overall aggressive variance of \$1.8 million. This amount is deemed acceptable.
CDO Liquid Indices EUR	ITRX_XS2_EUR_CONS.EUR.SENIOR_MMR_L.DERIV	D	IND001	97	(705)		(705)	Business has overall aggressive variance of \$0.1 million. This amount is deemed acceptable.
				(25,867)	626	(26,493)		
<i>Asia</i>								
Credit Structured Products	SANYO	2	MV	39,186	1,451		1,451	Broker quotes are not available for this position. Actual variance is 3.7%.
Credit Structured Products	PHILIP	D	CS01	82	1,323		1,323	Actual variance is 16.1 bps.
IRP - Derivatives Options	Interest Rate Volatility	D	Vol + 1%	17,332	(2,555)	(2,555)		Marked.
IRP - Derivatives Options	JPY Interest Rate Delta	D	PV01	9,826	(2,161)		(2,161)	Variance is due to curve construction differences. Lehman curve is based on FRA (floating rate agreements) up to the 6-month point while Totem uses deposit rates.
FX	FX options	D	Vol + 1%	4,873	(1,438)		(1,438)	Variance was discussed with the desk. PCG will continue to monitor and will further escalate if variance persists.
Commodities	Crude Oil Delta	D	PV01	5,833	(2,099)	(2,099)		Marked.
				(5,480)	(4,654)	(825)		
Total Significant Variances				(1,920,599)	(1,225,701)	(694,898)		

LEHMAN BROTHERS

PRICING REPORT – Cash Products Coverage

\$'000 Exposures	Level 1		Level 2		Level 3	
	MV	Coverage	MV	Coverage	MV	Coverage
CASH PRODUCTS						
Listed interest rate futures	(19,190,279)	98%	0		0	
Listed government bond futures	1,525,787	100%	0		0	
Commodity futures	(67,159)	100%	0		0	
Listed interest rate options	43,932	100%	0		0	
Listed bond options	13,468	100%	0		0	
Stocks and stock indices	238,019	88%	153,023	92%	6,623	0%
Listed stock & index futures	(46,609)	98%	0		0	
Listed stock & index options	19,751	90%	0		0	
Government bonds	(16,196,977)	100%	2,588,008	99%	0	
Inflation indexed bonds	0		0		0	
Corporate bonds	0		6,583,512	88%	164,614	97%
Convertible bonds	0		215,307	73%	324,852	83%
Money market instruments	0		6,060,980	100%	0	
RMBS bonds	0		0		0	
RMBS loans	0		4,262,365	99%	3,019,151	87%
Residuals	0		0		1,289,687	60%
CMBS bonds	0		11,721,556	30%	252,650	100%
CMBS loans	0		13,619,527	100%	2,559,654	100%
ABS bonds	0		6,239,672	96%	5,565,479	98%
CDS on ABS	0		(2,036,842)	99%	0	
HG business loans	0		1,435,784	100%	0	
Loans - secondary	0		9,567,217	80%	710,865	71%
Loans - in syndication	0		25,564,462	87%	267,554	100%
Firm relationship loans	0		6,050,351	96%	0	
Cash CDOs	0		648,637	99%	279,833	98%
Principal transactions	0		1,163,422	0%	13,037,281	98%
Private equity investments	0		0		1,975,179	49%
Non-performing loan portfolios	0		0		2,474,642	62%
Structured Notes	0		0		0	
Agency CMO bond	0		13,232,882	98%	0	
Pass throughs	0		493,501	100%	0	
Servicing rights	0		1,699,146	100%	0	
Preferreds	0		475,027	1%	0	
Muni bonds	0		5,513,286	96%	0	
Ascots	0		0		0	
Fund units	0		258,980	100%	0	
Warrants	0		382	100%	0	
Prime	0		3,575,109	100%	220,363	100%
Non prime	0		1,157,438	100%	56,100	100%
NIM	0		0		114,389	100%
TOTALS	(33,660,088)		120,242,733		32,318,914	

PRICING REPORT – Derivative Products Coverage

DERIVATIVE PRODUCTS \$'000							
RATES PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE	HYBRIDS PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE
Interest rate delta	PV01	11,811	100%	IR v FX correlation	Correl + 1%	0	
Inflation delta	PV01	(4,374)	97%	IR v commodity correlation	Correl + 1%	0	
Interest rate volatility - ATM	Vol + 1%	30,373	94%	IR v equity correlation	Correl + 1%	0	
Interest rate volatility - vol of vol (eps)	Vol + 1%	1,517	61%	Credit v inflation correlation	Correl + 10%	0	
Interest rate volatility - ir vol correlation (rho)	Vol + 1%	(3,955)	0%	Equity v FX correlation	Correl + 10%	0	
IR v IR correlation	Correl + 1%	0		Inflation v equity correlation	Correl + 1%	0	
IR v inflation correlation	Correl + 1%	0		Commodity v equity correlation	Correl + 1%	0	
Inflation volatility - ATM	Vol + 1%	0		FX v commodity correlation	Corr + 10%	0	
Inflation volatility - skew	Vol + 1%	0		Property derivatives	PV01	122	89%
CMS correlation - ATM	Correl + 10%	0		LBT index trades	Duration	0	
CMS correlation - skew	Correl + 10%	0		Balance guaranteed swaps - interest rate risk	PV01	0	
Basis swaps	PV01	(2,523)	94%	Balance guaranteed swaps - prepayment risk	Prep01	0	
				Balance guaranteed swaps - default risk	Def01	0	
CREDIT PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE	BMA trades - interest rate risk	PV01	(38)	100%
Credit spreads	CS01	(12,889)	81%	Credit v equity correlation	Correl + 10%	0	
Index spreads	IND001	(3,479)	95%	Credit v inflation correlation	Correl + 10%	0	
Tranche spreads	TR01	203	100%	Credit v interest rate correlation	Correl + 10%	0	
NTD basket correlation	Correl + 1%	(3,020)	76%				
Recovery rates	Recovery + 1%	6,737	84%	COMMODITY PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE
Credit volatility	Vol + 1%	51	91%	Metals - delta	PV01	(1,987)	100%
Corporate bond option delta	PV01	1,338	100%	Metals - ATM volatility	Vol + 1%	937	99%
Corporate bond option volatility	Vol + 1%	7,179	91%	Metals - skew	Vol + 1%	0	
Loan CDS	MV	0		Oil - delta	PV01	2,013	97%
CPPI volatility	Vol + 1%	1	56%	Oil - ATM volatility	Vol + 1%	(758)	97%
CPPI NAV	MV	0		Oil - skew	Vol + 1%	(480)	100%
CPPI jump rates	MV	0		Emissions - delta	PV01	(1,081)	99%
				Emissions - ATM volatility	Vol + 1%	7	0%
EQUITY PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE	Emissions - skew	Vol + 1%	0	
Single stock volatility	Vol + 1%	0		Power - delta	PV01	(526)	96%
Stock index volatility	Vol + 1%	0		Power - ATM volatility	Vol + 1%	0	
Dividend rho	D Rho	0		Power - skew	Vol + 1%	(1,595)	72%
Equity v equity correlation	Correl + 10%	1	100%	Natural gas - delta	PV01	(21,304)	100%
Equity delta	Pos delta	0		Natural gas - ATM volatility	Vol + 1%	0	
				Natural gas - skew	Vol + 1%	4,743	100%
FUNDS PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE	Refined products - delta	PV01	0	
Fund volatility	Vol + 1%	(3,027)	100%	Refined products - ATM volatility	Vol + 1%	0	
Fund vol of vol	Vol + 1%	(144)	100%	Refined products - skew	Vol + 1%	0	
IR v Fund NAV correlation	Correl + 20%	(2,802)	100%	Softs - delta	PV01	59,435	96%
Fund vol v NAV correlation	Correl + 20%	838	100%	Softs - ATM volatility	Vol + 1%	(99)	87%
Fund options NAV	Delta +/- 5%	2,084	100%	Softs - skew	Vol + 1%	0	
				Commodity indices - delta	PV01	439	96%
FX PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE	Commodity indices - ATM volatility	Vol + 1%	(4,749)	82%
FX delta	MV	(181,473)	100%	Commodity indices - skew	Vol + 1%	0	
FX forwards	PV01	3,157	100%	Commodity vs commodity correlation	Correl + 10%	0	
FX volatility - ATM	Vol + 1%	(10,728)	82%	Coal - delta	PV01	18	96%
FX volatility - skew	Vol + 1%	4,872	77%	Coal - ATM volatility	Vol + 1%	0	
FX barriers	PV01	0		Coal - skew	Vol + 1%	0	
FX v FX correlation	Corr + 10%	0		Uranium - delta	PV01	(208)	100%
				OTHER PARAMETERS	RISK MEASURE	NET EXPOSURE	COVERAGE
				Alltax swaps	PV01	1,872	100%
				Asset swaps	PV01	0	
				Mortgage volatility	MV	606,402	65%

PRICING REPORT – Projects

Business Line	Products	Contact Person	Region	Raising Issue	Risk of Misstatement (H/M/L)	Proposed Solution	System Enhancement Required (Y/N)	Due Date	Comment	Mitigating Controls (if any)
IRP	Caps	Yong Huang	NY	Need to assess cap vols skew p/l impact	H	Currently using Markt, however we are not calculating/reporting any p/l impact of using independent volatilities	Y	3Q08	Working with IT to perform full re-pricing of the entire portfolio	
IRP	Caps and Swaptions	Yong Huang	NY	For cap and swaption volatility skew testing, need to switch to new model that the desk recently implemented.	H	Working with Quan Research and desk to revise calibration for new model.	N	3Q08	Able to test European swaption with new model. Working on threshold.	
IRP	Exotics	Yong Huang	NY	Deal review processes are not in place for exotics	M	Establish deal review processes for exotics	N	3Q08		
IRP	Exotics	Yong Huang	NY	Need to expand both IRP and FX exotics submission and price testing	M	Expand Totem usage.	N	3Q08		
IRP	Options	Yong Huang	NY	Need to develop better methodology for the price testing of Bermudan and American options	M	Need to utilize Totem to test Bermudan options	Y	3Q08	Submitted to Totem the pricing of Bermudan options. Working on price testing methodology. Need to clarify model issues.	
IRP	General	Yong Huang	NY	Need to expand overall price testing coverage	M	Expand broker coverage	N	3Q08	Expanding broker coverage will be a continual process	
IRP	General	Yong Huang	NY	Need to improve the monitoring of variances	M	Implement variance time series tracking	N	3Q08		
FX	Options	Yong Huang	NY	Skew testing for FX trades that are greater than 2 years - testing 63 pairs right now	M	Need automation on manual testing.	Y	3Q08	Need IT improvements & increase number of currency pairs tested.	
FX	Baskets	Yong Huang	NY	Need to expand all correlation parameters (including currency pairs)	M	Need to utilize Totem to test correlation inputs	N	3Q08	Already established price testing on 50% of currency pairs; continue to expand coverage.	
Commodities	Eagle	Yong Huang	NY	Eagle price testing starts late in the month due to lack of resource for coverage	M	Will visit Houston to get to know key stake holders. NY team has conducted several PT on the portfolio, made new progress each time but still not complete due to lack of resources. As India team is trained up, certain LB price testing will be shifted in a controlled fashion to direct more and more NY resources to develop price testing on Eagle's portfolio.	Y		Currently price and position are sent by Eagle via email spreadsheet, hard to interpret. Once PC complete the position integration into Kinetic, will include Eagle in the normal process. In the interim, will work to get better position information out of Eagle's portfolio.	
Commodities	Exotics	Yong Huang	NY	Heat rate and other structure transaction testing; no third party quotes available currently	M	Continue working with Totem and 10x, develop and implement methodology to soR test heat rate deals, sensitivity analysis, monthly reconciliation b/t model and actual performance, historical correlation analysis, etc.	N			
Commodities	Basket	Yong Huang	London	Basket correlation testing; UK currently does not have a robust methodology	M	NY will work with UK to understand the Totem process, desk process and develop methodology and potentially take over the testing to NY	N			
Commodities	General	Yong Huang	NY	Asia price testing is currently handled by product control in Singapore, no dedicated local resource responsible	M	NY valuation control will take over entire Asia price testing from product control in Singapore	N			
Commodities	General	Yong Huang	NY	Price shape tracking: Price shape needs to be monitored	M	Develop and maintain tracking mechanism	N			
Commodities	General	Yong Huang	NY	Skew surface tracking: Skew surface needs to be monitored	M	Develop and maintain tracking mechanism	N			
Commodities	General	Yong Huang	NY	Structured portfolio is price tested with greeks as given, alternative procedure can be set up to test the sensitivity of inputs on greeks output	M	Develop and implement methodology in NY once more routine price testing gets transferred to India	N			
Commodities	General	Yong Huang	NY	Key risk locations are not tested with ideal frequency due to resource constraint	M	Educate India team to carry out ad hoc price verification on key risk locations	N			
Commodities	General	Yong Huang	NY	10x data is not used sufficiently in price testing due to lack to resource before	M	Resource constrain in NY prevent us from fully utilize 10x data. As India team get trained up, will utilize more on 10x return	N			
Commodities	General	Yong Huang	NY	Currently not involved in NPC items in UK	M	Coordinate with UK to get on European NPC agenda.	N			

PRICING REPORT – Projects

Business Line	Products	Contact Person	Region	Raising Issue	Issue	Risk of Misstatement (H/M/L)	Proposed Solution	System Enhancement Required (Y/N)	Due Date	Comment	Mitigating Controls (if any)
Securitized Products	CDX and Corp CDS	Joe Sapia	NY		Positions are not being price tested	H	A work flow for CDX and Corp CDS price testing is being developed. The SP positions should be included in the price testing that is performed by the Credit Valuations Team	N	TBD		
Securitized Products	Prime Whole Loans	Joe Sapia	NY		Need to implement model to value whole loans based on discounted cash flows	L	Continue to test the SPIRE model.	N	08/31/08		We currently still have sales activities that we price test to.
Securitized Products	Derivatives	Joe Sapia	NY		Automate the delivery of consensus pricing to MarkIt and Fitch.	L	RAMP data automation project completed with Mortgage Analytics team. The project should further enhance our existing relationship with MarkIt for a stronger partnership in derivative pricing. Successfully delivered the daily automation feed from RAMP to MarkIt's server.	N	07/31/08		
Securitized Products	Mortgage Servicing Rights	Joe Sapia	NY		Prices not reflecting slower CPR in the market.	H	MSR valuation models used in RAMP were updated to reflect slower prepayment speeds as experienced in the market.	Y	TBD		
Securitized Products	Non Cash Flow Positions	Joe Sapia	NY		Appropriate price testing method needs to be developed.	M	NCF positions will continue to be researched.	N	Ongoing		
Securitized Products	All	Joe Sapia	NY		Eliminate manual file preparation	M	Automation of Ramp synthetics file	N	08/31/08		
Securitized Products	All	Joe Sapia	NY		Preparing FAS157 data is inefficient.	H	Automation of the FAS157 template is being developed in order to reduce the time needed to prepare the data.	N	08/31/08		
Credit	CDO	Scott Goswami	Global		Global Deal Review backlog is 250 trades	H	4 out of 5 staff hired in India. Training is ongoing. 2008 headcount under discussion	N	Ongoing	Backlog reduced to 164 trades by 31-May-08 (Q2)	10% of P&L held back against incomplete reviews
Credit	CDS	Scott Goswami	NY		CDS price testing dbase creates artificial variances and is extremely inefficient to use	H	IT headcount approved and in place. Project plan yet to be completed and approved to use	Y	TBD	All fixes for cds to be completed by 31-Jul-08. Ongoing development to expand the dbase functionality to all credit parameters to be completed by Nov-08	
Credit	CDS on ABS	Scott Goswami	NY		CDS on ABS is not price tested	H	Should be tested by ABS Val team as they have a better knowledge base and expertise	N	TBD		
Credit	Equities and ABS	Scott Goswami	NY		Products such as equities and ABS are tested by GCP Val team.	L	Identify products and discuss outsourcing with other teams	N	3Q08		
Credit	General	Scott Goswami	NY		Global Valuation reporting to be created for Management review	M	Create reports and distribute to Desk heads	N	3Q08		
Credit	General	Scott Goswami	NY		Price testing policy documents need to be unified across products and regions	L	One detailed FV policy should be written and approved by PC and the Desk. Should include thresholds, categorization of variances and data, escalation procedures, etc	N	3Q08		
Credit	General	Scott Goswami	NY		Control to be put in place to monitor stale marks	L	Begin monitoring the CDS tool. Look into creating a bond tool which monitors spreads	Y	TBD	CDS Resolved. Reports sent out monthly. Bonds yet to be addressed	
Credit	General	Scott Goswami	NY		Inadequate control in place to enforce "one firm one mark" policy	L		Y	TBD		
Credit	General	Scott Goswami	NY		Valuation reports are completed after day 20 of the month. This limits exposure, relevance, and our ability to resolve issues. It also reduces time for value added projects.	H	Evaluate requirements, build a price testing database, stream line inefficiencies and redundancies, prioritize components of PV, train staff, and hire new staff	Y	TBD		
Credit	General	Scott Goswami	NY		Ensure all valid and reliable pricing sources are utilized.	M	Research the quality of current and new data sources. Incorporate into testing and categorize. Build a database to compile data efficiently	Y	3Q08		
Credit	General	Scott Goswami	NY		Incorporation of recent trade prices into price testing work is extremely cumbersome and performed on a best effort basis when variances are large	M	Automated source to capture and incorporate into the price picking methodology	Y	TBD		
Credit	General	Scott Goswami	NY		Insufficient time spent on HG cash testing. Val risk has increased substantially over the last few months (SIV's, Auction Rate Sec, preffords, etc)	M	New staff to be hired and trained	N	TBD		

PRICING REPORT – Projects

Business Line	Products	Contact Person	Region Raising Issue	Issue	Risk of Misstatement (H/M/L)	Proposed Solution	System Enhancement Required (Y/N)	Due Date	Comment	Mitigating Controls (if any)
Real Estate	Derivatives (Duration Neutral Swaps / TRS)	Abe Kebede	NY	Cleaning up unexplained reserves from year-end	M	Performing weekly testing and reconciliations, working with middle office to resolve trade booking issues	Y	2Q/3Q/08	Product control working with front office, middle office and technology teams, Using Ramp as a calculation engine for daily MTM and P&L calculations	
Real Estate	Floating Rate Large Loans & Junior Notes	Abe Kebede	NY	Floating rate securitization market is inactive; No deal in the market since Dec-07. Spreads published in third party publications are stale; Pricing becoming extremely challenging	M	Working with Front Office to obtain market color on deals that are currently in the market for syndication / sale.	N	Ongoing	Product control is having continuous discussions with Front Office going through deals in more detail and trying to obtain market color by using recent syndications, bids, offers and any other market information.	Significant amount of asset sales in Q208 provided some market color and it was used in completing our Q2 reviews
Real Estate	PTG	Abe Kebede	NY	Valuation methodology with Servicer for development-type assets outdated.	M	Discussions started with Front Office Asset Management and Risk Management to implement changes	N	3Q/4Q08	Current valuation methodology for land and development projects is based on cap * 105%, which was a conservative or prudent approach in an up-market. Given current market conditions, this approach may not be appropriate.	Trimax (our main servicer) is developing IRR models and walking away from cap * 105% methodology
Commodities	Basket	Rob Honeyball	London	We do not have greeks for correlation and therefore are unable to quantify a price testing variance	M	Need to source greeks. Requires tech and quant work.	Y	To be scheduled		
Commodities	Basket	Rob Honeyball	London	We do not have greeks for correlation and therefore are unable to accurately reserve against this.	M	Need to source greeks. Requires tech and quant work.	Y	To be scheduled		
Commodities	Options	Rob Honeyball	London	We cannot see skew positions in Kineticx and therefore cannot assess untested population	M	Need to source greeks. Requires tech and quant work.	Y	To be scheduled		
Commodities	Options	Rob Honeyball	London	We cannot see skew positions in Kineticx and therefore where we do believe risk to be significant and do try to test the process is horribly manual, time consuming and error prone.	M	Need to source greeks. Requires tech and quant work. Additionally some work to automate the submission / testing process can be done to free up resource.	Y	To be scheduled		
Commodities	Correlation	Rob Honeyball	London	Correlation time-series is flat (e.g Dec 8 correlation = Dec 10 correlation for each pair). That is not appropriate in some instances.	M	Need to source greeks so we can assess risk and reserve accordingly.	Y	To be scheduled		
Commodities	Exotic Commodity Trades	Rob Honeyball	London	Exotics outside of Kineticx are not price tested	M	Integration of models into Kineticx via Flexdeal and model approval process.	Y	Ongoing		
Commodities	Commodity Options and Baskets	Rob Honeyball	London	Do not have the ability to effectively price test correlation and volatility surfaces due to the number of curves.	M	Currently developing IT solution to automate the process of submitting curves to consensus survey.	Y	To be scheduled		
Commodities	Commodity Options and Baskets	Rob Honeyball	London	Untested inventories on: 1) illiquid or long-dated positions, 2) index atm volatilities and 3) agricultural atm volatilities	L	Currently, methodology is slowly being developed for each product. Need to add headcount to expedite the process.	N	Ongoing as markets develop and new underliers are added.		
Credit	CDO Tranchelets	Tony Ellis	London	Tranchelet risk not fully tested	L	Analysis vs Totem consensus data	N	3Q08	Totem Consensus data received but not used in price testing	
Credit	PO Liquid Tranches	Tony Ellis	London	PO levels not fully tested	M	Participate in Proposed Totem service	N	3Q08	Current price testing done on a risk basis. Good as proxy but price basis preferable	Currently tested on risk basis
Credit	Credit Swaptions	Tony Ellis	London	Only make a basic submission to Totem / limited results	L	Staff training and meetings with Totem to understand their pricing process	N	3Q08	Complete submission made for Jun-08 service. Expected completion in Q3 08	Basic price testing shows conservative variance, good coverage
Credit	Derivatives on CLOs/CDOs	Tony Ellis	London	Coverage/Methodology to be improved	M		N	3Q08		
Credit	Super Senior CDO Tranches	Tony Ellis	London	Super senior levels not fully tested	M			TBD		
Credit	CLO/CDO Residuals	Tony Ellis	London	Coverage/Methodology to be improved	M			TBD		
Credit	High Yield	Tony Ellis	London	Loan CDS not price tested	L	Need to follow up.	N	TBD	Working on getting external data from both FitchSolutions and Markit.	

PRICING REPORT – projects

Business Line	Products	Contact Person	Region Raising Issue	Issue	Risk of Misstatement (H/M/L)	Proposed Solution	System Enhancement Required (Y/N)	Due Date	Comment	Mitigating Controls (if any)
Securitized Products	Residuals	Tony Ellis	London	Residuals policy to be developed	L	In development	N	TBD		
Securitized Products	Non Performing Loans	Tony Ellis	London	Income recognition policy to be developed. Limited price testing done.		To send income recognition policy for review.		TBD	This is written - can send for review	
Securitized Products	Structured Finance	Tony Ellis	London	Some structured trades booked at transaction price and cash accounted.		Spread look trades do not have available curves. Need to follow up.		TBD		
Securitized Products	CDS on ABS	Tony Ellis	London	CDS on ABS is not price tested	H		TBD	3Q08	Working on getting external data from both: FitchSolutions and Markt.	
IRP	Fund Derivatives	Tony Ellis	London	Gap Option Volatility untested	H	Based on historical vols and index cliquet options. Possible Totem service to be set up	N	3Q08		
All	All	All	London	Proof of price testing population completeness and integrity needed in many areas	M	Developed standardized template which has now been put into production	N	3Q08	Completed for CTE, Vanilla Rates completed but not yet rolled out due to resource limitations in the line, other products TBD	
All	All	All	London	Ongoing (i.e. post model review) calibration controls to be developed (global project)	M	Develop methodology	Y	TBD		
All	All	All	London	Need to assess significance of exposure where Markt offer service but we don't subscribe - e.g. CMA, inflation exposures	L	Research Lehman products as well as what Markt offers. CMS now subscribed to CDS and CDO, ABS in future, not yet subscribed on Markt.	N	TBD		
All	All	All	London	Need to ensure that all significant factors relevant to valuation are identified and covered	M	Credit perceives no issues	N	N/A		
All	All	All	London	Need to develop full repricing methodology	M	Credit: Develop methodology IRP: Rates repricing being built in Optmodel Commodities: Develop Policy	Y	TBD	Credit: Not yet key priority in credit Commodities: To be included in the revamp of the policies generally by end of 1Q08	
All	All	All	London	Alternative procedures to justify acceptance of marks on untested exposures need to be more precise.				TBD	Being assessed through VCO review of PT templates	
All	All	All	London	Model reserve assessment to be completed in many areas	M	Work in Progress	Y	TBD		
All	All	All	London	FAS157 level 1, 2 and 3 classification of asset types to be concluded and embedded in price testing templates (global project)		Tagging process ongoing, correct assignment of exposures to levels in PT templates needs proper line manager review		TBD		
Credit	High Yield (CBs, Bonds, Private Equity, Warrants, Loans)	Atul Sethi / Jose Galvan	Tokyo	Coverage/Methodology to be improved. Most of the positions are in emerging market and privately placed with no publicly available market information. It is difficult to find comparable benchmarks.	H	Since Q3, we have started to have formal detailed discussion with desk on all material positions. The discussion is around actual financial performance of the investee vis-a-vis expected performance, performance of credit indices, IPO plans (if any) and refinancing. We are interviewing for a Credit Valuation role and the new person would focus on the valuation of credit portfolio.	N	TBD		
Credit	High Yield (CBs, Bonds, Private Equity, Warrants, Loans)	Atul Sethi / Jose Galvan	Tokyo	Valuation reports are completed after day 20 of the month. This limits exposure, relevance, and our ability to resolve issues.	H	Evaluate requirements, stream line inefficiencies and redundancies, prioritize components of PV and hire new staff		TBD		
Credit	Distressed Assets/ NPLs	Atul Sethi / Jose Galvan	Tokyo	Coverage/Methodology to be improved.	H	To have the new dedicated credit valuation resource to look at valuation of NPLs and other distressed assets. To do formal independent valuation analysis based on realised and expected cashflows.		TBD		