

LEHMAN BROTHERS HOLDINGS INC.
Minutes of the Audit Committee
July 22, 2008

A meeting of the Audit Committee of Lehman Brothers Holdings Inc. (the "Corporation", "Holdings" or, collectively with its subsidiaries, the "Firm") was held jointly with a meeting of the Audit Committee of Lehman Brothers Inc. ("LBI") in the Executive Conference Room, 31st Floor, 745 Seventh Avenue, New York, New York, on July 22, 2008, at 11:00 a.m., pursuant to written notice.

PRESENT - COMMITTEE MEMBERS

Messrs. Michael L. Ainslie
Roger S. Berlind
Thomas H. Craikshank (Chairman)
Sir Christopher Gent

ALSO PRESENT BY INVITATION

Messrs. John Akers
Clement Bernard
Neeraj Chopra
Martin Kelly
Ian Lowitt
Gerard Reilly
Ms. Beth Rudofker
Messrs. Thomas A. Russo
William Schlich (Ernst & Young)
Jeffrey A. Welikson

APPROVAL OF MINUTES

The first order of business was the approval of the Minutes of the meeting held on July 8, 2008. Upon motion duly made and seconded, it was unanimously

RESOLVED, that the Minutes of the meeting of the Audit Committee held on July 8, 2008 are hereby approved in the form submitted at this meeting, and that a copy of such Minutes be placed in the appropriate Minute Book of the Corporation.

VALUATION REVIEW

Mr. Reilly introduced the Valuation Review, stating that it would consist of an overview of the Product Control function, including valuation control; a review of the key functions performed by the Valuation and Control group within Product Control, including price testing and the determination of fair value level hierarchy; a review of mark to mark adjustments during the second fiscal quarter and the market events or transactions which drove those adjustments; and a review of the results of the valuation testing for residential and commercial mortgages and leveraged loans at the end of the second fiscal quarter.

Mr. Reilly then presented an overview of the Product Control function, describing its responsibilities for business analysis, business control, valuation control, and revenue transaction control. The Committee directed questions to management regarding the Product Control function, including its responsibilities, structure, reporting lines and independence from business units.

Mr. Chopra then described the Valuation and Control group. He described the group as consisting of technical staff who are very familiar with the products they cover and who are responsible for verifying prices for assets and liabilities, both on and off balance sheet. Mr. Chopra stated that prices are verified through data providers, consensus pricing services, extrapolation from similar instruments, and recent trading activity. He also noted that significant variances are then escalated to senior management for further consideration. Mr. Chopra described the model control process and the review of complex derivatives transactions. The Committee directed questions to management regarding the use of consensus pricing services and the role of Ernst & Young in auditing the valuations.

Mr. Chopra then discussed the responsibilities of the Valuation and Control group for assigning fair value hierarchy levels to the assets and liabilities and for completing the related disclosure requirements. Mr. Chopra provided a description of how the fair value hierarchy level for a particular asset is determined and outlined the relevant guidelines. The Committee directed questions to management about the fair value hierarchy, including the determination of the appropriate level for assets and the movement of assets between levels.

Mr. Reilly continued the presentation by discussing write downs and market events related to residential mortgages. He noted that gross write downs for residential mortgages in the second quarter were \$2.4 billion compared to \$3 billion in the first quarter. He described the Peloton default, a large non performing loan sale by the Firm, the loss related to swapping subprime securities out of a Firm-sponsored investment fund, and losses from poor credit performance and spread widening in the quarter. Mr. Reilly and Mr. Chopra then presented an analysis of the balance sheet position at the end of the second fiscal quarter, transactions which occurred during the quarter, and the results of the price testing by Product Control, for the Firm's U.S. and European residential mortgages. The Committee directed questions to management regarding the Firm's valuation of residential mortgages and pricing developments in the third fiscal quarter to date.

Mr. Reilly then discussed the write downs and market events that have taken place with respect to leveraged loans. He noted that the Firm took gross write downs of \$300 million on leveraged loans during the second quarter compared to \$700 million in the first quarter. Mr. Reilly described the Firm's bulk sale of Home Depot Supply and losses based on price transparency from the syndication process on several other issues. He also provided a roll forward analysis of the Firm's leveraged acquisition financing for the first two fiscal quarters of 2008.

Mr. Chopra then detailed price verification methods for acquisition facilities and described how the Firm utilizes four basic price verification methods: (1) external quotes; (2) trading activity; (3) CDS matrix; and (4) CR matrix. He provided details on the aforementioned methods and other price verification methods, including the price flex method applied to Archstone. Mr. Chopra then presented the results of the valuation testing for acquisition loan facilities at the end of the second quarter. The Committee directed questions to management regarding the results of the valuation testing for the second quarter.

Mr. Reilly continued the presentation by discussing the write downs and market events during the second quarter with respect to commercial real estate. He noted that the Firm took gross write downs of \$900 million in the second quarter compared to \$1.4 billion in the first quarter. He noted that floating rate commercial assets continued to weaken with spread widening leading to a loss of \$400 million in the quarter. Mr. Reilly stated that the Firm took write downs of \$500 million on Archstone and the SunCal portfolio. The Archstone write down was largely on the bridge equity, which has not been syndicated. The SunCal portfolio consists of 24 residential land development projects, primarily located in Southern California, and the write down was due to the weakness in the residential market in that area. The Committee directed questions to management regarding a recent press article on the Firm's investment in SunCal.

Mr. Chopra then detailed price verification methodology with respect to commercial real estate, noting that price verification is performed on a monthly basis and that, generally, third party pricing inputs are used where available. He stated that the Firm's principal book is price verified using a NPV approach with a significant emphasis on the credit qualities of each collateral. Mr. Chopra detailed how the Firm's models use:

- Property level information provided by third party servicers (Trimont and PCCP)
- Discount rates that are derived from third party publications (Institutional Investors' Real Estate Finance & Investments)
- Product Control, which reviews IRR models developed for each position for reasonableness

Mr. Chopra noted that bridge equity is generally marked to target investor yields for the specific investment and that Product Control reviews the reasonableness of the valuation assumptions. Mr. Chopra also detailed how the commercial real estate book is price verified using internal models based on spreads obtained from third party publications, giving special emphasis to recent sales, circles and bids on notes of similar attributes. He also described how

Product Control discusses with business senior management pricing variances that exceed the Firm's established thresholds. Mr. Chopra then presented an analysis of the balance sheet position at the end of the second quarter and sales which occurred during the quarter, for the Firm's U.S., European and Asian commercial real estate positions. The Committee directed questions to management regarding this analysis, third quarter developments, and conditions in the European and Asian commercial real estate markets.

Messrs. Bernard and Chopra were excused from the meeting.

EUROPEAN EQUITY VOLATILITY REVIEW

Ms. Rudofker reported on the results of the investigation and control review related to the valuation discrepancy in the European Equities Volatility business identified during the first quarter. As background, she noted that the control infrastructure for the Equity Volatility business was assessed as a Sarbanes-Oxley significant deficiency in 2006 and 2007. She noted that while progress was made in 2007, improvements were still required in 2008 to avoid a material weakness assessment. Ms. Rudofker described the Firm's response to the valuation discrepancy in the European Equities Volatility business identified during the first fiscal quarter of 2008. She reported that the Firm immediately suspended the senior trader and his supervisor, focused on determining the correct pricing methodology and valuation, informed Ernst & Young and the Firm's regulators of the incident, and commenced an independent internal review. Ms. Rudofker reported that Corporate Audit has completed this review, reviewed the findings with management and agreed to a set of control improvements that must be made during 2008 in order to avoid a material weakness under Sarbanes-Oxley, satisfy regulatory expectations, and assist in dealing with regulatory inquiries. Ms. Rudofker then reported that these control improvements, together with individual responsibility, completion dates and standards have been committed to by management of the Front Office, Finance, Risk Management and Operations (Middle Office). She stated that the findings and action plans have also been reviewed with Ernst & Young and all open audit findings and action plans are part of the business infrastructure improvement project. The Committee directed questions to management regarding the consequences to the employees directly involved in the issue, their reporting line, and other matters.

EMPLOYEE LETTER REVIEW

Ms. Rudofker summarized the review conducted in response to a letter that was received by senior Finance and Risk Management personnel of the Firm from an employee in the Finance department responsible for Global Balance Sheet and Legal Entity Accounting. The employee's letter indicated that he had concerns related to balance sheet and legal entity controls for which he was responsible. Ms. Rudofker noted that this letter was sent only a few days prior to the Firm's May reduction-in-force and at the time the letter was sent, a decision had already been made to eliminate this employee's position as part of the reduction-in-force and restructure his role to address enhancements that had been identified. Ms. Rudofker stated that she and the Firm's General Counsel and Ernst & Young had met with the employee numerous times to discuss the points the employee raised, including meetings between Ernst & Young and the employee at which management was not present. She reported that Corporate Audit has largely completed, in partnership with Financial Control and Ernst & Young, an evaluation of the

concerns raised by the employee. Ms. Rudofker stated that no material issues have been identified during the review and she summarized certain of the findings and recommendations and distributed a detailed report. She noted that the controls for which this employee was responsible are important secondary controls, but are not relied upon as part of Sarbanes-Oxley audit testing due to previously identified gaps. Mr. Cruikshank emphasized the importance of thoroughly investigating every concern raised by the employee.

PRIVATE SESSION

The Committee met privately with Ernst & Young. The Committee then met privately with Ms. Rudofker.

There being no further business, upon motion duly made and seconded, the meeting was adjourned.

Respectfully submitted,

Jeffrey A. Welikson
Jeffrey A. Welikson
Secretary