

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’

9 (a) 9 (c)



For tri-party the Euroclear ‘re-use’ option is active

For equity securities we ensure that voting rights have been transferred

9 (b)



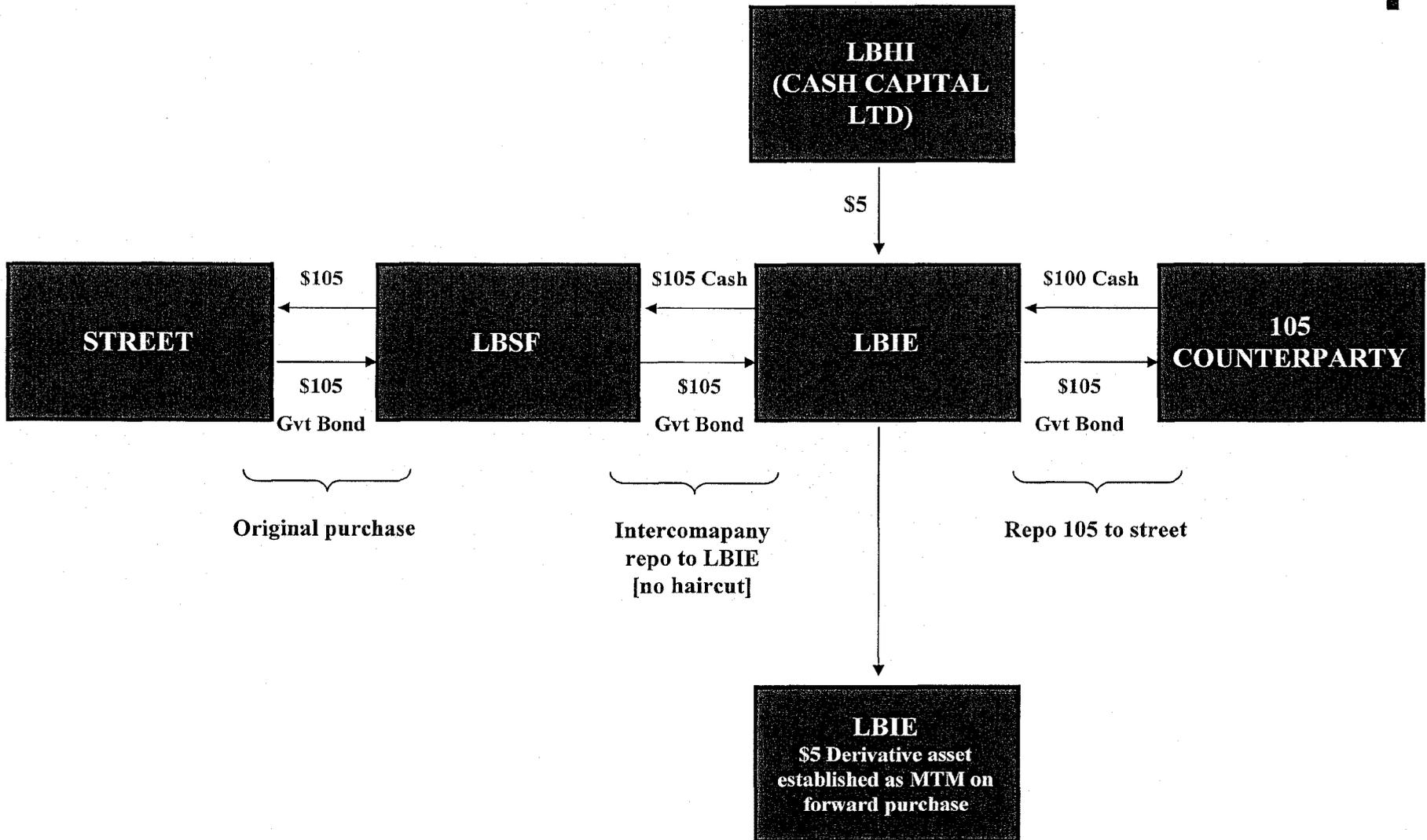
Above normal market haircut
105% for Fixed Income and
108% for Equities

Additional haircut implies that we have insufficient cash to repurchase assets and therefore they are ‘sold’

9 (c)



Example Flow Diagram



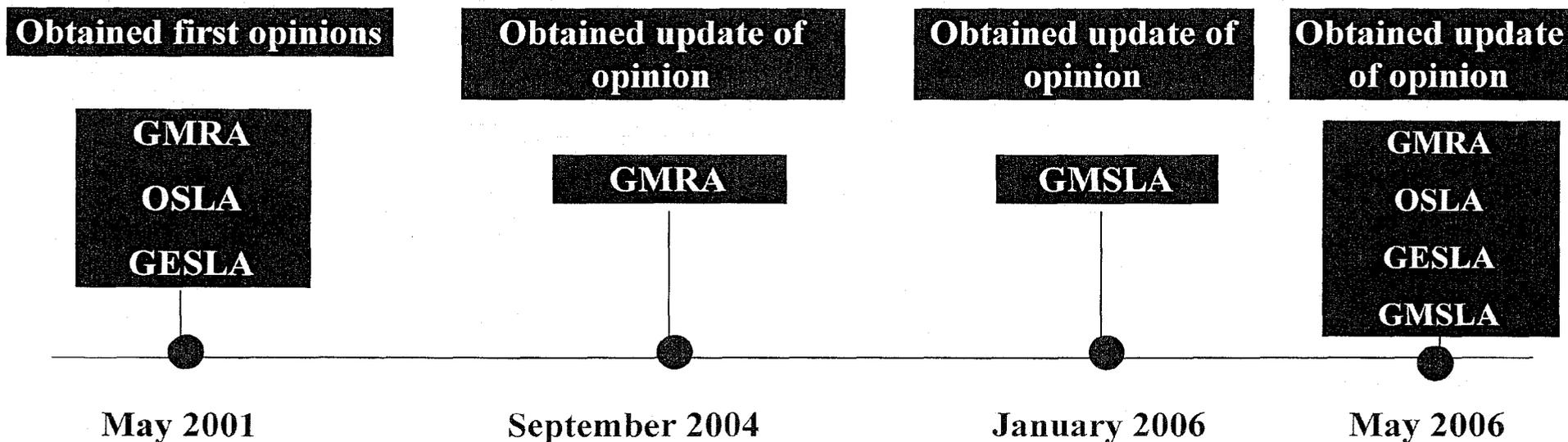
Operating Rules

- **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

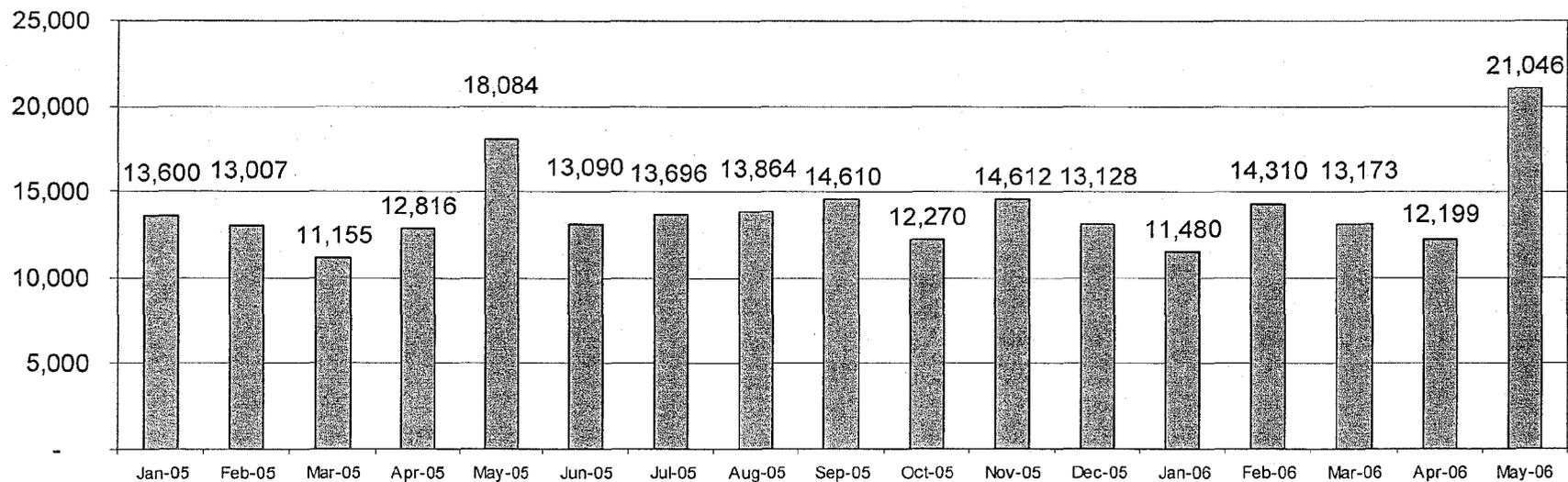
- ◆ Agreements are in place with the following organizations:
 - GMRA (Global Master Repurchase Agreement)
 - OSLA (Overseas Securities Lending Agreement) – never used
 - GESLA (Master Gilt Edged Stock Lending Agreement) – never used
 - GMSLA (Global Master Securities Lending Agreement) – never used



Monthly Trend

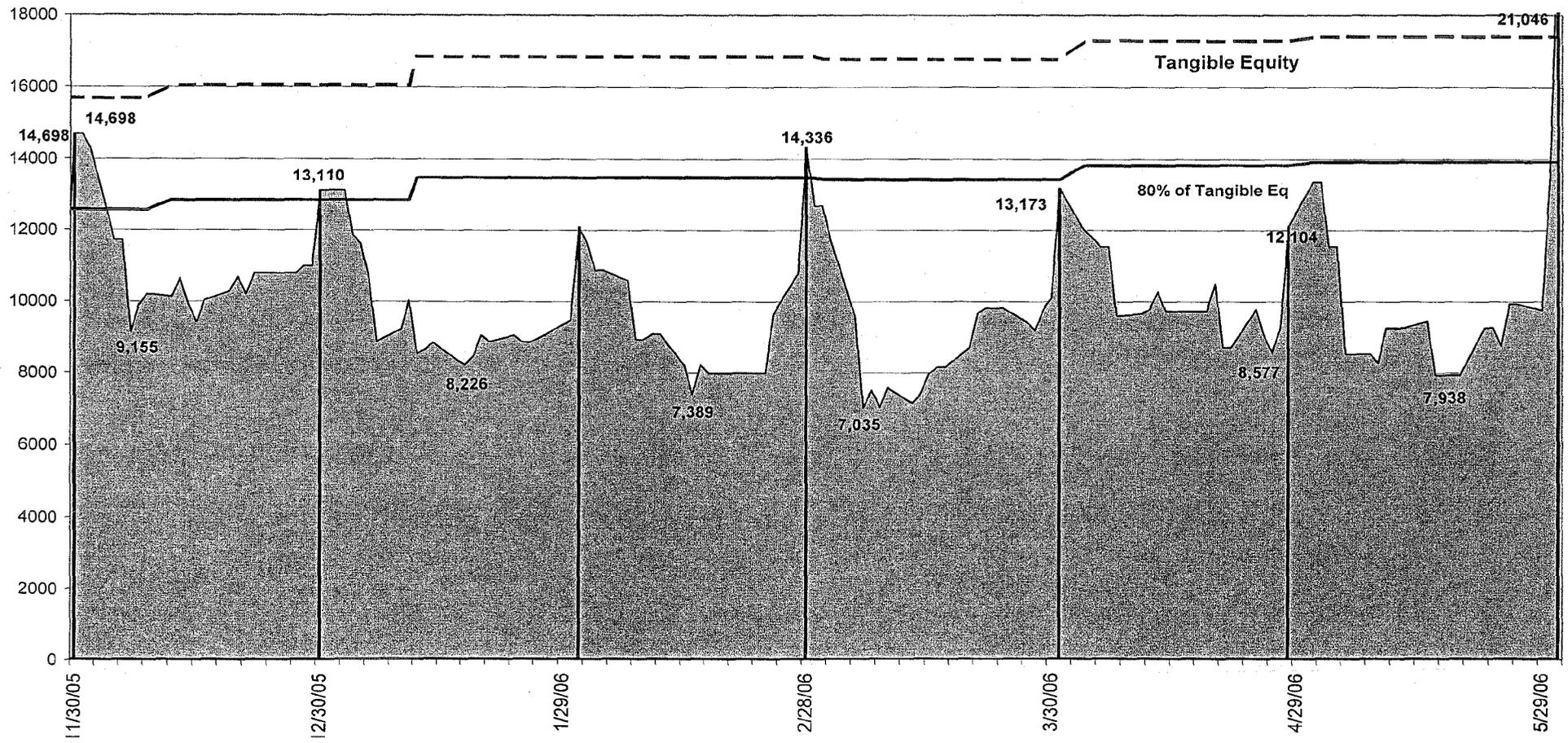
- ◆ Total Repo 105 usage reached a record high of \$21B for May quarter end
- ◆ Repo108 for equity securities was introduced as at May 2006 [\$0.6B]

REPO 105 Month – End Trend
\$ Million



Daily Trend

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



Business Benefit

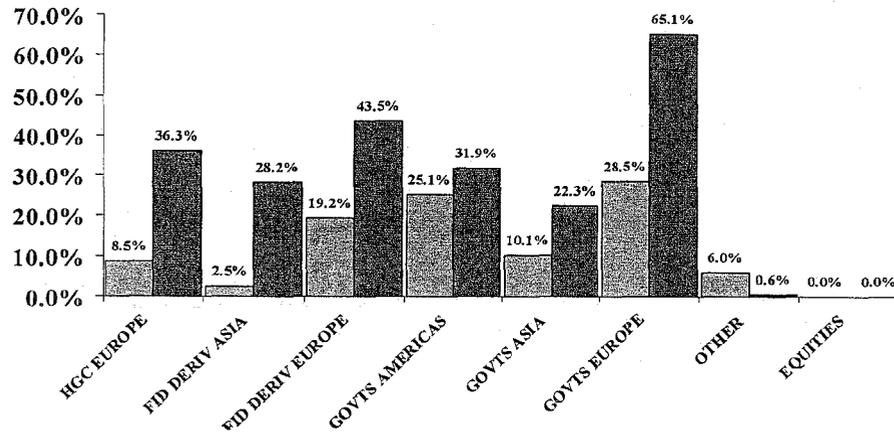
November 2005

\$14.6B

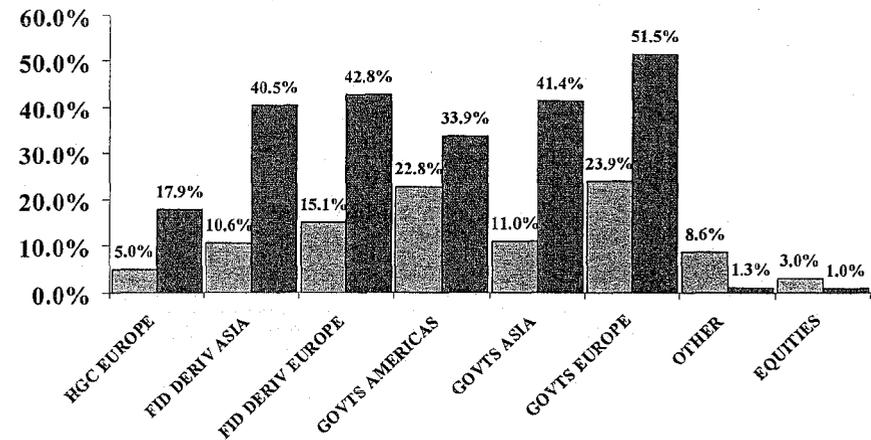
May 2006

\$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



Who uses Repo 105 ?

Goldman Sachs **x**

Merrill Lynch **?**

Morgan Stanley **✓**

Bear Stearns **✓**

JP Morgan Chase **x**

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]