

## SEC Talking Points:

### I. APPROACH / INTRODUCTION

- As you are aware, we have been working on a number of initiatives to stabilize Lehman's marketplace standing and to restore the confidence of our clients, counterparties and shareholders
- To date, there remain influential market participants that do not believe we have taken sufficient steps to reduce the perceived risks on our balance sheet, and this continuing perception has negatively impacted our stock price
  - One specific concern that has been repeated is that we are not selling or otherwise reducing our exposure to our commercial real estate assets quickly enough
  - However, engaging in a "fire sale" of these assets at severely depressed prices could result in further value destruction, rather than value creation; additionally, many other institutions have similar assets and such sales would negatively impact their carrying value as well as future sale values
- Our objective is to find a solution that reduces the risk on our balance sheet, but maintains the upside in our commercial real estate portfolio for our shareholders
  - We believe that the true value of these assets is greater than their current marks
- The solution we would like to discuss today is the creation of a new entity, SpinCo, whose assets will consist of approximately \$[25 – 35] bn of our commercial real estate assets
  - SpinCo equity securities will be distributed to Lehman shareholders, creating a standalone commercial real estate entity
  - Lehman will initially provide necessary debt financing to SpinCo; it is expected that SpinCo will obtain external debt financing from other sources at a later point
  - It is expected that Lehman will not consolidate SpinCo, achieving our goal of reducing perceived balance sheet risk
  - SpinCo will be managed on a portfolio basis to maximize the return to shareholders, achieving our goal of allowing our shareholders to participate in the upside of our commercial real estate assets
    - Rather than the near-term "fire sale" scenario, SpinCo manager will have the flexibility to sell assets or hold them to maturity – whichever alternative offers a greater return to shareholders

- In addition, it is expected that we, Lehman, will raise additional equity capital to replenish some of the equity distributed as part of SpinCo, although timing is yet to be determined
  - The distributed equity will not be replaced on a dollar-for-dollar basis as Lehman will no longer be supporting the commercial real estate portfolio
- The success of the transaction and its potential to have a positive reception in the marketplace will largely depend on the ability to execute as quickly as possible
- We need to be in a position to announce a plan of action with regard to our commercial real estate assets on our upcoming earnings call in mid-September
  - A very near-term announcement (i.e, in connection with our third quarter earnings announcement) is important to us for several reasons
  - Our clients, counterparties and shareholders, as well as a broader spectrum of market participants, are looking for us to present a clear path through these difficult markets
  - Announcing a spin in connection with the third quarter earnings provides the following benefits:
    - Preserves shareholder value and marketplace standing for Lehman
    - For counterparties, allows Lehman to be viewed as a strong and stable counterparty on a going forward basis
    - Helps alleviate some of the perceived uncertainty regarding the U.S. financial system more generally
- However, we cannot announce the spin-off on our September earnings call without confidence that we can execute the transaction within a short time frame post-announcement
  - A key to having that confidence is to be comfortable that we can complete the SEC review process relatively quickly
  - Current internal goal is to complete the spin-off by our fiscal year end (November 30)
  - Interim tasks are primarily operational in nature or related to obtaining third-party transfer consents (where necessary)
- In order to achieve this timeline, we will need the cooperation and support of the SEC – with respect to two specific items in particular, which we will discuss in detail

## **II. SPINCO OVERVIEW**

### ***Structure Overview***

- We have spent a significant amount of time examining potential corporate structures for SpinCo
- The two primary alternatives are a C-Corp and a publicly traded partnership (PTP)

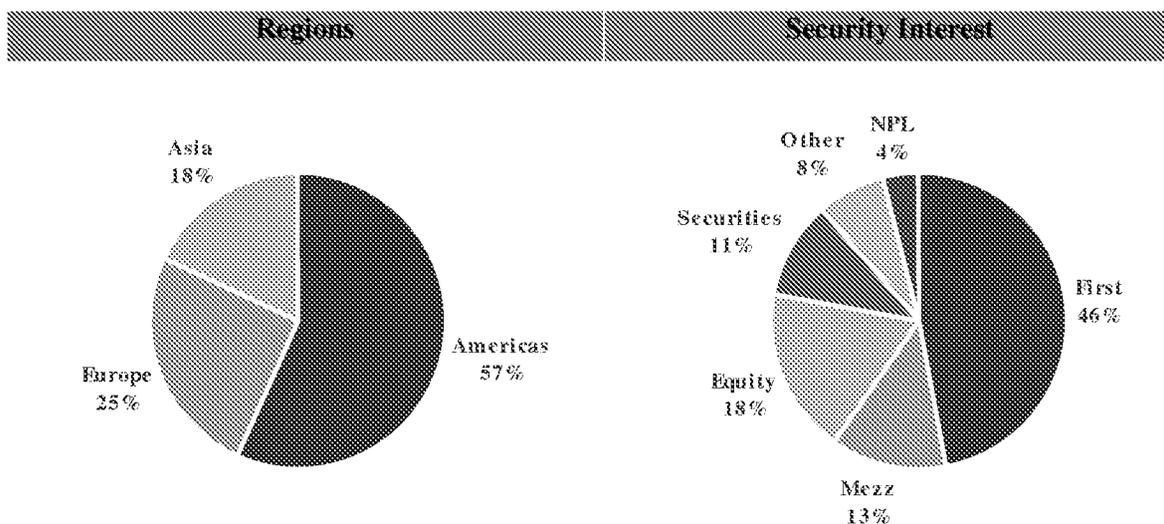
- Key differences between C-Corp and PTP are largely tax-related
  - With a C-Corp:
    - We may be able to structure the transaction to be tax-free to shareholders
    - However, there will be corporate level tax paid on future earnings
  - With a PTP:
    - Spin-off will likely be taxable to shareholders as a dividend
    - However, no corporate level tax on a substantial portion of future earnings

**Governance Overview**

- SpinCo will be either internally or externally managed and have its own Board of Directors and executive officers
- The manager of SpinCo will not be Lehman or any of its affiliates

**Asset Overview**

- SpinCo is currently being organized – the assets to be contributed to SpinCo are currently owned across a large number of domestic and foreign Lehman subsidiaries



- Overview of indicative portfolio concentration
  - 2,603 positions
  - Average position size of \$15.3 mm
  - Largest position is approximately 15% of total portfolio (Archstone, based on gross balance sheet exposure as of 5/31/08)

**Capitalization Overview**

- It is expected that SpinCo will have approximately \$[25 – 35] bn in assets

- Portfolio size will ultimately depend upon a number of factors including potential pre-spin sales of assets, legal restrictions on the transferability of specific assets and appropriate capitalization of SpinCo
- Absolute sizing of equity and debt portions of capital structure will depend upon size of asset portfolio
  - Expected to be approximately 30% equity and 70% debt
    - For example, a \$35 bn asset portfolio would have:
      - Approximately \$10 bn of equity
      - Approximately \$25 bn of debt
- We expect SpinCo to have interest coverage of:
  - Approximately 5.5x
  - Approximately 1.0x, excluding expected loan repayments
- Lehman is expected to hold a significant portion of the debt, and potentially all of the debt, at the time of spin
- Lehman does not expect to consolidate SpinCo

***Business Plan Overview***

- The objective is to reduce the risk to Lehman's balance sheet while preserving the upside of the commercial real estate portfolio for shareholders
- SpinCo will selectively monetize assets where it believes it is maximizing value to shareholders
  - Maximize recovery for at least a 10% IRR on the assets
  - Potentially build out projects if doing so maximizes proceeds and returns over the long term
- Manage liquidity prudently such that any covenant or maturity breach is addressed early
- Selectively re-invest equity released in existing assets if it enhances shareholder value
- Potentially raise additional institutional capital at the asset level or at the SpinCo level if it enhances liquidity and returns to shareholders

**III. REQUESTS TO SEC**

**A. Expected Presentation of Financial Information**

- We request that SpinCo not be required to present historical financial information
- We strongly believe this information is not relevant to investors and that the appropriate financial presentation would include (1) a current, audited opening balance sheet, (2)

prospective financial statements (subject to “agreed upon procedures” from our auditors) and (3) detailed tabular information regarding the assets

- Let us explain the rationale for this conclusion:
  - Historically, virtually all of our real estate assets were managed on a discrete and transitory basis
  - The assets were acquired and are held by various domestic and foreign subsidiaries of Lehman and have not been, and it previously was not expected that they would be, administered as a whole or in significant groups
  - In contrast, spin-offs customarily involve separating a discrete business segment or business operation that has a meaningful operating history – this is vastly different – there is no operating history and the assets being brought together we acquired and managed separately
  - In addition, because these assets were acquired and managed on a disparate basis, financial statements do not exist for the assets as a whole or any significant subset of the assets
  
- To provide additional context for why we believe the financial presentation we expect to furnish is appropriate and why we believe the relief we are requesting should be granted, let us (1) provide some background on how market realities have significantly affected our approach to managing our real estate assets and (2) share with you some statistics that demonstrate that this is a “new” entity where historical financial statements are not relevant or material
  - Until recently, in the ordinary course of their businesses, various Lehman subsidiaries acquired numerous real estate assets that, in the majority of instances, were resold or transferred shortly thereafter in whole or in part in connection with a wide array of transactions, including bridge equity syndications and debt securitizations
  - The expected asset pool is both vast and diverse
    - Approximately \$[25 – 35] bn portfolio
    - Approximately 2,603 positions with an average size of \$15.3 mm
    - 57% U.S., 25% European, 18% Asian
  - In the current environment, many of these syndications are not available and we do not expect them to be available in the near term

- As a result, we believe the return to shareholders on our real estate assets we currently hold will be maximized by pooling the assets and managing that pool over a longer term. In essence, taking assets acquired at various times and for various purposes and contributing them to a new entity to be managed in accordance with the current market conditions
- With respect to our current real estate assets – the ones we expect to be held by SpinCo – these were originated and/or purchased at various points in time with approximately 50% acquired in the past year and 80% acquired in past two years
- In light of these factors – the diversity of the characteristics of the assets, the fact that historically the assets have been managed separately and resold within a short period, and the change in how we expect them to be managed going forward – we have concluded, and our outside accountants and legal advisors agree, that historical financial statements would not be relevant or meaningful to investors
- We also note that, even if we were to go down the road of attempting to prepare historical financial statements, because of the diversity of the characteristics of the assets and how they have been managed, there is no accounting predecessor to use as a starting point in preparing financial statements
  - In reaching our conclusion we focused on what information is relevant to investors - to protect them and allow a transparent market to develop in the securities of SpinCo
  - It is critical to us that the market has the information it needs to efficiently trade these securities and to allow investors to make an informed investment decision
  - As it relates to historical financial information, this situation is more akin to asset-backed securities offerings, which do not include historical financial statements
  - We would compare the analysis we believe is relevant to the analysis performed to determine if an acquisition constitutes the acquisition of a business for purposes of Article 11 of Regulation S-X – applying that facts and circumstances analysis to the assets to be contributed to SpinCo, we come to the clear conclusion that the assets to be contributed to SpinCo are not a business and pro formas and separate financials would not have to be presented by an acquirer

- As we outlined at the outset, we are asking for relief from the historical financial requirement (3 years of audited financial statements and 5 years of selected financial information) for SpinCo and focusing instead on the information that is relevant and material to investors:
  - Current audited, opening balance sheet
  - Prospective financial statements (subject to “agreed upon procedures” from our auditors)
  - Detailed tabular information on the assets
  
- A directly relevant precedent that we have found was Kearny Street Real Estate Company in 1993; we note that Grant Street (OTS supervision) also used a similar model
  - Bank of America established Kearny Street to purchase loans and real estate assets from Bank of America with proceeds of an equity investment and the issuance of notes registered with the SEC
  - The SEC gave Kearny Street relief similar to what we are seeking
  - Given the unique facts of our situation and the fact that the only similar precedent we are aware of occurred fifteen years ago, granting a waiver should not set a difficult precedent
  
- If the requested relief is granted, SpinCo will not have 2008 financial statements
  - As a result, SpinCo quarterly filings in 2009 will contain financials for the relevant 2009 period, but will not contain a comparison to the corresponding 2008 period
  - The first Form 10-K with audited financials will be for fiscal year 2009
  
- There are other practical considerations that are motivating our request for relief
- In the event that we are required to provide 3 years of audited historical financials, even if we were able to form a basis for constructing these statements, we expect it would push timing back to at least Summer 2009 and make an announcement on the September earnings call significantly less meaningful and less effective at addressing our issues
- For the reasons mentioned earlier, we believe it is in the best interests of our clients, counterparties and shareholders to announce this transaction as soon as practicable and ensure that execution occurs shortly thereafter

**B. Expedited Process**

- As we mentioned earlier, we would like to make an announcement about our commercial real estate assets in conjunction with our earnings release in September
- We are requesting a response to our requests as soon as practicable

- This would provide us with an appropriate amount of time to evaluate our alternatives in the context of your response, present the alternatives to our Board of Directors and work on the filing
  
- Current internal goal is to complete the spin-off by our fiscal year end (November 30)
- Therefore, we would also request the ability for SpinCo to file its initial Form 10 without financials on which E&Y will have completed its agreed-upon procedures to streamline the process
  - Auditors can perform those agreed upon procedures while the SEC reviews the body of the Form 10
  - Subsequent filing of the Form 10 would include the audited opening balance sheet and agreed-upon financial information