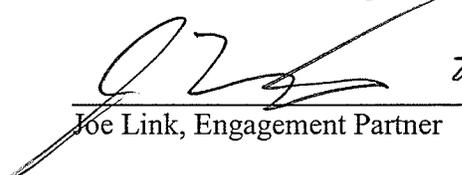


**Lehman Brothers Holdings Inc.
Summary Review Memorandum
Consolidated Financial Statements
Quarter-ended May 31, 2008**

Prepared by:

 8/8/08 a/o 7/10/08
Stavros Zafiridis, Manager

Reviewed by:

 7-8-08 as of 7/10/08
Joe Link, Engagement Partner

Approved by:

William Schlich, Coordinating Partner

Approved by:

Paul Haus, Independent Review Partner

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Summary Review Memorandum
Consolidated Financial Statements
Quarter-ended May 31, 2008**

Prepared by:  8/5/08 also 7/10/08
Stavros Zafiridis, Manager

Reviewed by:  3-8-08 09 of 7/10/08
Joe Link, Engagement Partner

Approved by: _____
William Schlich, Coordinating Partner

Approved by:  8/22/08
Paul Haus, Independent Review Partner

Summary Review Memorandum

Scope

Our timely quarterly review of Lehman Brothers Holdings, Inc.'s ("LBHI", "Lehman", or the "Company") unaudited interim consolidated financial statements as of and for the three and six-month periods ended May 31, 2008 is performed in accordance with standards established by the Public Company Accounting Oversight Board (United States). Our procedures consisted principally of applying analytical review procedures and making inquiries of persons responsible for financial and accounting matters. A review is substantially less in scope than an audit conducted in accordance with standards established by the Public Company Accounting Oversight Board (United States). The objective of our review of the Company's interim financial information is to provide us with a basis for communicating whether we are aware of any material modifications that should be made to the Company's interim financial information for it to conform with generally accepted accounting principles.

Results

The Company reported a net loss of \$2.7 billion and a net loss per share of \$5.14 for the three month period ended May 31, 2008 as compared year over year to net income of \$1.2 billion and diluted earnings per share of \$2.21. For the six-month period ended May 31, 2008, the Company reported a net loss of \$2.3 billion and a net loss per share of \$4.33 as compared year over year to net income of \$2.4 billion and diluted earnings per share of \$4.17. The decrease primarily reflects negative valuation adjustments made to various asset classes (see *Impact from Market Related Events* for further details).

Significant Accounting and Auditing Issues**Impact from Market Related Events***Significant Write-downs/ Valuation of Financial Instruments*

Overview

During the second quarter of FY 2008, the credit markets continued to decline as a result of the credit and liquidity crisis. As a result, the Company continued to record negative valuation adjustments on certain components of its financial instruments. In addition, the results were impacted by the ineffectiveness of the Company's risk mitigation strategies. The net amount of valuation adjustments in the first quarter FY 2008 was an approximate \$3.6 billion reduction to the Company's net revenues.

In billions	Three Months Ended		Six Months Ended	
	May 31, 2008		May 31, 2008	
	Gross	Net ⁽¹⁾	Gross	Net ⁽¹⁾
Residential mortgage-related positions	\$(2.4)	\$(2.0)	\$(5.4)	\$(2.8)
Other asset-backed-related position	(0.4)	(0.4)	(0.6)	(0.5)
Commercial mortgage and real estate-related investments ⁽²⁾	(0.9)	(1.3)	(2.3)	(2.3)
Acquisition finance facilities (funded and unfunded)	(0.3)	(0.4)	(1.0)	(0.9)

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	(4.0)	(4.1)	(9.3)	(6.5)
Valuation of debt liabilities ⁽³⁾	0.4	0.4	1.0	1.0
	<u>\$(3.6)</u>	<u>\$(3.7)</u>	<u>\$(8.3)</u>	<u>\$(5.5)</u>

(1)The net impact represents the remaining impact from the components after including the impact of certain economic risk mitigation strategies. The gross impact excludes any effect of economic risk mitigation strategies.

(2)Certain real estate-related investments are reflected as a component of Real estate held for sale. The Company makes equity and debt investments in entities (including voting-interest entities and VIEs) whose underlying assets are real estate. The Company consolidates those entities in which it either controls the entity under SFAS 94 or is the primary beneficiary in accordance with FIN 46(R). The Company does not have economic exposure to the total underlying assets in those entities. The amounts presented are the Company's net investment and therefore exclude the amounts that have been consolidated but for which the Company does not have economic exposure. Other asset categories, not included in this table, also contain interests in entities that engage in real estate-related activities.

(3)Represents the gain on debt liabilities the Company elected to measure at fair value under SFAS 159. These gains represent the effect of changes in the Company's credit spread and exclude any interest income or expense as well as any gain or loss from the embedded derivative components of these instruments. Changes in valuations are allocated to the businesses in relation to the cash generated by, or funding requirements of, the underlying positions.

Mortgage Related Positions- (Residential, Commercial, etc.)

Mortgage Related Positions- (Residential, Commercial, etc.)

Overview

The impact of the credit crisis and the resulting changes in market risk perception and liquidity has continued to result in adverse conditions in the broader global financial markets including the US housing market, commercial real estate, global investing and short-term liquidity.

Following 160bps decreases in the Fed Funds rate during 1Q08, the Fed Funds rate again dropped a full 100bps to 2.00% in response to adverse market conditions and broader market factors, including the purchase of Bear Stearns by J.P. Morgan Chase and the opening of the Fed Funds window to non-IDI brokers and dealers of securities and investment banks. In securitized products, spreads on agency and prime conventional fixed 30 year products have narrowed slightly while ABX 07-2 spreads on AAA ABS and AAA CMBS have continued to widen. Also, spreads related to Real Estate assets have widened during the quarter across various property types.

During the quarter Lehman sought to reduce its exposure to these asset classes as well as part of the firm's overall initiative to reduce leverage.

Securitized Products

In 2Q 2008, Lehman's Principal transactions from securitized products was a loss of \$(2.0)bn as compared to a loss of \$(636)mm in Q108 and a \$48\mm gain in 2Q07. The business recorded mark-downs of approximately \$2.4bn on its residential mortgage portfolio, of which approximately \$890mm pertain to losses on U.S prime (primarily ALT-A) bonds, residuals, and NIMs while U.S. subprime write downs approximated \$756mm for the quarter. Additionally, approximately \$168mm of write-downs related to CDOs, approximately \$250mm related to write-downs on positions collateralized by European assets, approximately \$105mm related to commercial real estate assets in the Securitized Products business unit and approximately \$256mm related to other asset backed securities including ABS new issues and ABS secondary trading. Lehman's P&L from mortgage related derivatives, primarily index trades and single name credit default swaps, went from a gain of approximately \$2.2bn in 1Q08 to a gain of approximately \$400mm in Q2 2008 as the hedges

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became less effective due to changing correlations between index bases and spreads relative to cash product spreads.

Lehman's global mortgage origination volumes were down during 2Q '08 (63% vs. prior quarter and 96% vs. prior year comparable period), primarily as a result of Lehman's decision to exit the sub-prime and wholesale prime origination business in late 2007 and early 2008, respectively.

Lehman's residential loan securitization business continues to incur losses in 2Q08 as approximately \$10bn of securitized notional was executed at an average yield of -43bps for a loss of \$(43)mm compared to approximately \$7.6bn of securitized notional, -42bps yield, and a loss of \$32mm in 1Q08 and approximately \$56bn of securitized notional, +31bps yield, and a gain of \$19mm in the year-ago period. This statistic illustrates the nature and extent of the changes in the securitized products marketplace from the year-ago period.

Our analysis and procedures for the review of the balance sheet as of 5/31/08 and the related income statement accounts during our 2nd quarter review consisted principally of the following: 1) Analytical procedures designed to address changes, or unexpected lack of changes, in key balance sheet and revenue captions within the Securitized Products business unit, 2) Reviews of significant P&L items including write-downs, realized transactions, and securitizations 3) Review of the results of Product Control's price verification procedures for significant product groups, including whole loans, MBS/ABS securities, mortgage servicing rights, and other products, 4) Review of a sample of significant positions and/or exposures to product classes, 5) Review and comparison of recent, relevant trade history to current pricing for asset classes with trading activity and/or the ABX index pricing(ex. Whole Loans, MBS/ABS), 6) Review of Quest Footnotes, other adjustments, and deferrals, and 7) Review of available and applicable market research and peer disclosures for comparison, as relevant. Together, these procedures are designed to provide review and analysis of both material net revenue items as well as the significant transactions, exposures, and pricing that affect the balance sheet and financial results of the Securitized Products business unit.

Commercial Real Estate

Principal transactions from Commercial Real Estate ("CRE") for the quarter ended May 31, 2008 resulted in a loss of approximately \$1.5bn, down approximately \$1.9bn from 2Q '07 and \$420mm from 1Q '08. Continued declines in CRE revenues are the result of a combination of significant reductions in deal activity and valuation deterioration in certain areas in the US and Europe as market conditions and the lack of liquidity continue to negatively impact the commercial real estate markets. While the second quarter of 2008 saw increased activity in asset sales, transaction prices continue to reflect lower market valuations due to market liquidity and risk premiums associated with CRE financing. While the CMBS market has not shown defaults similar to that of the securitized products market, uncertainty about macroeconomics and liquidity have contributed to wider spreads and decreased liquidity in the formerly robust market. Quarterly losses primarily reflect the impact of continued write-downs across multiple areas of the CRE portfolio in both the US and Europe, while CRE performance in Asia remains stable.

Lehman recorded approximately \$1.1bn (\$900mm with consideration of \$200mm of net gains) in mark-downs for the quarter on the global CRE portfolio, with most of the mark-downs on positions backed by U.S. based land and condominium assets (\$325mm) with other significant mark-downs in

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bridge equity positions, including the Archstone Smith facility, (\$349mm) and Other PTG, US commercial loans, and European commercial loans and CMBS (\$420mm). Further, Lehman completed one U.S. based commercial securitization in 2Q08 with a \$200mm notional at a realized spread of -200bps from book value for a loss of \$10mm. Contrastingly, in 1Q08 Lehman recorded no commercial securitizations and in the year-ago period recorded three transactions with \$5bn of notional, a realized spread of 150bps and gains of \$76mm.

Similar to hedging and other trading activities in securitized products, Lehman also carries positions such as credit default swaps, interest rate swaps, and in the CMBX. However, hedging activities resulted in a net loss of approximately \$223mm (\$400mm with consideration of the aforementioned \$200mm included in the gross amount) compared to approximately \$400mm of gains in 1Q08 and immaterial net hedge P&L from the year-ago period. Real estate derivative revenues were immaterial in 1Q07. The decline in the current quarter was primarily the result of ineffectiveness of the hedges as Lehman utilizes derivatives whose underlying is and index based of fixed rate commercial loans while its portfolio is primarily floating rate commercial loans and large single asset positions.

Our analysis and procedures for the review of the balance sheet as of 5/31/08 and the related income statement accounts during our 2nd quarter review consisted principally of the following: 1) Analytical procedures designed to address changes, or unexpected lack of changes, in key balance sheet and revenue captions within the Commercial Real Estate business unit, 2) Reviews of significant P&L items including write-downs, realized transactions, and securitizations, 3) Review of the results of Product Control's price verification procedures for significant product groups, including Commercial Loans, PTG Debt & Equity positions, and Commercial Derivatives, 4) Review of a sample of significant positions and/or exposures to product classes, 5) Review and comparison of recent, relevant trade history to current pricing for asset classes with trading activity, 6) Review of Quest Footnotes, other adjustments, and deferrals, 7) Review of analyses and estimates related to financial reporting of certain positions and transactions using applicable authoritative accounting guidance (ex. FIN 46, FAS 144, FAS 140) and 8) Review of available and applicable market research and peer disclosures for comparison, as relevant. Together, these procedures are designed to provide review and analysis of both material business unit balances and income/expenses as well as the significant transactions, exposures, and pricing that affect the balance sheet and financial results of the Securitized Products business unit.

Valuation of Contingent Acquisition Facilities

Lehman's Contingent Acquisition Facilities ("CAF") are comprised of the following:

In billions	May 30, 2008	February 29, 2008
High grade:		
Contingent	\$ 1.7	\$ 7.2
Unfunded	1.1	0.8
Funded	3.6	2.9
	\$6.4	\$ 10.9

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High yield:		
Contingent	\$.425	\$ 3.7
Unfunded	2.1	2.2
Funded	9.0	11.9
	\$11.52	\$ 17.8

Contingent Commitments

Lehman provides contingent commitments to investment and non-investment grade counterparties related to acquisition financing. Actual funding of these contingent commitments is dependent upon both a proposed transaction being completed as well as the borrower fully utilizing Lehman's commitments (rather than using other financing sources within the capital markets). As of May 30, 2008, the contractual committed amount of Lehman's global contingent acquisition commitments was \$2.12bn, as compared to \$10.9bn as of February 29, 2008. Contingent commitment activity during the quarter was as follows:

- \$3.9bn in deals completed, resulting in a decline in high grade and high yield commitments. The related LBO debt was either syndicated or retained in Lehman's inventory (funded and unfunded bank loans)
- \$4.8bn in deals that fell through or are currently in the litigation stage, and therefore Lehman's contingent commitment has ceased.
- \$0.92bn decrease in Lehman's commitment due to other banks joining the syndication group and therefore taking on a portion of Lehman's commitment
- \$0.93bn in new contingent commitments extended during the quarter

We note that Lehman's \$2.12bn contingent acquisition commitment inventory as of May 30, 2008 typically contain MAC clauses (a contingent borrower's ability to draw on the commitment is subject to there being no material adverse change in the borrower's financial condition) and flex pricing terms (flexible pricing features to adjust for changing market conditions prior to closing).

In accordance with the AICPA Audit and Accounting Guide, Brokers and Dealers in Securities, Lehman accounts for all its lending commitments at fair value, with changes in fair value recorded in earnings.

Unfunded and Funded Leveraged Loans

Once the M&A contingency is realized, it is Lehman's intent to distribute this leveraged debt through syndication. However, Lehman may not be able to syndicate the full lending facility because of market conditions. Additionally, Lehman may extend lending facilities to counterparties for business relationship purposes. As of May 30, 2008, the contractual committed amount of Lehman's global leveraged loans (funded and unfunded) was \$11.5bn, as compared to \$17.8bn as of February 29, 2008.

Q2 08 CAF Valuation and YTD Writedowns

During the second quarter of FY 2008, the illiquidity in the capital markets continued and syndication activity was limited. As a result, Lehman compared its global commitments and loans to updated return expectations, resulting in a gross unrealized loss, net of underwriting fees, hedge gains and carry, of approximately \$(300)mm. This gross calculation is conservative, as it does not factor in the probability that the deal will close at the stated term, as many of these commitments will expire unused. Management then estimated the amount of underwriting fees to be recognized when/if the deal is closed, along with LCDX hedge revenues and carry on closed deals, and net these amounts against the \$(300)mm, resulting in a net loss of \$(400)mm at May 30, 2008. Due to spreads tightening and ongoing

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market conditions losses were realized on these hedges for Q2 2008. Losses on hedges comprised of \$93mm in Americas, and \$32mm in Europe. The netting of expected underwriting fees within Principal Transactions against the CAF write downs is consistent across the industry.

The weighted average price change in the High Yield portfolios went from 91.8 at February 29, 2008 to 88.1 at May 30, 2008, respectively. The largest writedowns in the quarter were taken on the following facilities (note: amounts represent unrealized losses, net of fees and carry): Applebees (\$128.2mm; average price of 91.00), Home Depot Supply (\$92.6mm; average price of 88.50), Hawaiian Telecom (\$77.4mm; average price of 78.50), and Houghton Mifflin (\$28.2mm; average price of 84.6).

We obtained Lehman's second quarter contingent acquisition commitment price verification analysis and discussed Lehman's independent price verification methodology with Product Control. The price verification process includes a variety of methods to independently substantiate the price at which each commitment has been marked, including recent trading activity, consensus quotes (obtained from LSTA), matrix pricing (CDS and CRA benchmarking). Based on our review, we did not note any major remarks or variances as a result of price verification performed by Lehman's product control group.

The fair value of Lehman's leveraged loan facilities is estimated using executed transactions on comparable loans, market price quotations (Mark-it Partners consensus quotes) and market observable credit default swaps.

As a result of our review procedures, we conclude that Lehman's CAF valuations appear reasonable as of May 30, 2008.

Valuation of Other Asset-backed (non residential)

Given the lack of liquidity in the Cash CDO market, Lehman experienced continued mark downs in its CDO business during the first quarter of 2008. As of May 30, 2008 and February 29, 2008, the market value of Lehman's global Cash CDO inventory totaled \$1.5 billion and \$2.1 billion respectively. The \$1.5 billion was comprised of \$ 526 million of sub-prime and \$974 million of corporate-backed CDOs.

The significant decrease in Lehman's global Cash CDO inventory was due to the liquidation of Corona Borealis CDO Ltd with reference obligations as Residential Mortgage Backed Securities ('RMBS'), Commercial Mortgage Backed Securities ('CMBS'), CDO securities, and other asset backed securities. Lehman held several pieces of Corona. The majority of what was held in Lehman's inventory was the super senior tranche – Class A1-A in the amount of \$0.75bn. As of May 2, 2008 Corona Borealis CDO Ltd was one of the many Asset Backed Securities (ABS) CDOs that experienced an event of default (EOD). During this time of default an 'acceleration notice' was received by Standard & Poor's. In this case the controlling shareholders voted to accelerate the maturity of the CDO notes outstanding. On May 14, 2008 the CDS agreement was terminated and all required CDS Termination Payments were made to the Credit Default Swap Counterparty (Lehman Brothers Special Financing Inc. (LBSF)). On May 15, 2008 LaSalle Global Trust Services (trustee of Corona) held a public auction of the remaining collateral debt securities. On May 22, 2008 proceeds of the liquidation were distributed to asset classes. After liquidation, Lehman realized a \$7.6m loss resulting from hedge remarks, swaps being unwound in conjunction with the trust, and settlement of all collateral.

Of Lehman's sub-prime backed CDO exposure, approximately \$0.85 billion was related to a AAA super senior position related to the Ceago Deal backed by high grade collateral and marked at 57% as of May 30, 2008 compared to price of 64% as of February 29, 2008. Given the current lack of liquidity for super

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senior CDO positions, Product Control took the approach of price verifying each of the underlying collateral in the Ceago CDO through third party quotes for getting comfortable with fair value of the Ceago position. No significant variances were noted between Front Office and Product Control's prices after considering valuation adjustments taken on these positions

We also reviewed Lehman's corporate-backed Cash CDO and CLO warehousing portfolio price testing, noting no significant price testing variances and consistency with the February 29, 2008 price testing process.

As a result of our review procedures, we conclude that Lehman's Cash CDO portfolio is fairly stated at May 30, 2008.

Structured Link Notes ("SLN's")***Background***

In connection with its adoption of SFAS 157, *Fair Value Measurements* ("SFAS 157") and SFAS 159, *The Fair Value of Option for Financial Assets and Financial Liabilities* ("SFAS 159"), Lehman elected to fair value substantially all structured linked notes ("SLNs") not previously accounted for at fair value under SFAS No. 155, *Accounting for Certain Hybrid Financial Instruments*—an amendment of FASB Statements No. 133 and 140.

Changes in the value of the Company's structured link note portfolio are driven by changes in the value of the Company's credit worthiness that are primarily driven by changes in the current term structure of Lehman credit spreads. Lehman measures the impact of the credit spread component by assuming that this component may be modeled as a fixed rate position (i.e. fixed leg of a swap) where the coupon is the credit spread. The change in component value is equal to the difference of the change in value of the credit spread as of the valuation date (discounted using the valuation date credit curve) from the NPV of the credit spread as of the issuance date, discounted by the issuance date credit curve. Please see the *2007 Consolidated SRM* for a detail explanation of the Company's process and valuation methodology relating to its SLN's.

Changes from Q1 2008

During the first quarter FY 2008, Lehman chose to construct its credit spread curve by obtaining bid and offer spreads from front office traders on various Lehman-issued index bonds in the market as of February 29, 2008, taking into account the volume and term structure of the issuance. Lehman used bid spreads over LIBOR rates as a proxy for credit spreads for their structured link note valuation model.

In the second quarter FY 2008, Lehman continued to construct its credit spread curve using the same methodology but changed the inputs used in the credit spread curve. In the prior quarter, Lehman obtained bid and offer spreads from front office traders on Lehman-issued index bonds in the U.S. market. In the current quarter, Lehman refined the inputs by obtaining bid and offer spreads that reflect Lehman-issued index bonds in the respective markets of the SLN's (US, Euro, and Bankhaus issuances) given the differentiation in spreads in the respective market. Lehman concluded that the refinement of the inputs better reflects the Company's credit spreads in its respective market based on trading activity.

The new inputs in the credit spread curves were constructed using the bid and offer spreads from U.S. issuances and is applied to the US SLN portfolio only. The Euro curve is derived from bid and offer spreads from front office traders on various Euro bonds in the market as of May 31, 2008 for the first ten

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years. Maturities beyond 10 years are extrapolated due to limited bond activity. The Bankhaus curve is derived from the Bankhaus issuance curve plus 20 bps for buybacks.

The following table summarizes Total P&L Effect and the breakup within the respective portfolios:

SLN Valuation	USD	EUR	Bankhaus	Total 2008 2 nd Quarter	2008 1st Quarter
Total Notional	\$21.6B	\$15.9B	\$1.1B	\$38.6B	\$38.4B
Weighted Expected Life	3.3	5.49	8.92	4.36	4.23
Weighted Spread Change	1.68	2.62	1.00	2.05	1.56
Total P&L Effect	\$0.87B	\$1.45B	\$0.05B	\$2.37B	\$1.95B

P&L Impact

As of 5/31/08, the total notional of structured debt fair valued by Lehman stood at \$38.6 billion. On a portfolio basis the above debt had a weighted expected life of 4.36 years with a weighted issuance spread of 41 bps and secondary spread of 246 bps thus resulting in net spread change of over 205 bps over the weighted expected life. This widening in credit spreads resulted in total P&L impact of \$2.37 billion for the quarter as compared to \$1.56 billion in the previous quarter. The following table summarizes changes in Notional/MTM over various quarters:

SLN Valuation	2008 Q2	2008 Q1	2007 Q4	2007 Q3
Total Notional	\$38.6B	\$38.4B	\$35.5B	\$31.5B
Weighted Expected Life	4.36	4.23	4.23	4.11
Weighted Issuance Spread	0.41	0.25	0.16	0.12
Weighted Secondary Spread	2.46	1.81	1.3	1.04
Spread Change	2.05	1.56	1.13	0.92
Total P&L Effect	\$2.37B	\$1.95B	\$1.35B	\$916.2M

EY Review Procedures

We performed procedures over the completeness of the SLN portfolio. We also performed a review over the underlying inputs and assumptions used in the model. We reviewed the application of the credit curve as well as overall analytics over the credit spread impact calculation and total P&L effect. In addition, we reviewed the additional top-side adjustments with P&L impact. Based on our work performed, we deem the total P&L effect during the quarter to be reasonable.

Conclusion

As a result of the procedures noted above, we concluded that the methodology applied for the credit spread impact on the Structured-Link Notes portfolio is reasonable. We are not aware of any modifications required to be made to the Company's valuation of the SLN's.

Auction Rate Securities

Auction-rate securities ("ARS") are typically long-term bonds with interest rates that reset periodically (usually once a month) at a Dutch auction. These securities have traditionally served as a means of connecting borrowers with long-term financing needs with investors who desire to hold short-term

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investments that can be readily turned into cash. Lehman and other investment banks hold regular auctions of these securities, allowing investors to roll the securities with new interest rates or to sell them to new investors. However, due to the recent disruption in the credit markets, investor demand for these securities has declined, as evidenced via the recent auction failures since the third quarter of 2007. When auctions fail, holders of these securities receive the maximum rate to compensate them for the fact that they now own long-term securities for which there is effectively no market.

As of November 30, 2007, Lehman's high grade auction rate securities portfolio was approximately \$2.8 billion which has grown to approximately \$6.7 billion as of February 29, 2008. As the auction facilitator, Lehman is not obligated to act as the liquidity provider, however it did buy a portion of these securities to facilitate market liquidity and maintain customer relationships. For the quarter, Lehman took an additional \$159mm in writedowns related to the auction rate securities.

Note: Q-o-Q change in MV in above table includes MTM changes and buybacks as of 2/29/08

KSK

KSK is a joint venture to build power plants in India in which the Global Trading Strategies business has a 33.425% stake. During the quarter the fair value of the investment decreased from \$714mm as of the end of Q1'08 to \$551mm as of the end of Q2'08. Approximately \$121mm in the change is related to a decrease in the mark from 289 Indian Rupees ("Rs") per share as of the end of Q1'08 to Rs240 per share as of the end of Q2'08. Approximately \$42mm of the change was caused a decrease in Rs from approximately Rs39.8 per \$1USD as of February 29, 2008 to Rs42.74 per \$1USD as of May 31, 2008. The FX loss on the Rs was off-set by a Rs FX macro-hedge which resulted in gains of \$38mm.

During Q1'08 KSK filed a draft red herring with an IPO anticipated for late Q2'08. A discounted cash flow was prepared which indicated that a strategic buyer would be willing to buy KSK for \$2.85 billion. After taking a 25% haircut for owning a minority stake the value of the Lehman's investment was determined to be \$714 million as of the end Q2'08, a \$550 million gain over the basis of \$160 million as of the end of Q4'07 and fees of \$4 million.

Beginning in early March, KSK received commitment letters from 4 investors to participate in a pre-IPO financing round. The commitments of Rs289-350 per share validated Lehman's mark as of the end of Q1'08. KSK did not draw on these commitments and decided to wait until closer to the IPO date to complete the pre-IPO financing. Due to significant declines in the India market during Q2'08, the IPO was projected as of the end of Q2'08 to be priced between Rs240-289 per share. Based on the projected IPO levels, the pre-IPO financing was completed on June 3rd at Rs240 per share, with six firms participating for \$17.3mm shares, a combined 5% stake.

Lehman's mark of Rs240 per share as of May 31, 2008 was consistent with the pre-IPO financing completed on June 3rd. Based on Lehman's 98.3mm shares at a mark of Rs240 per share and Rs42.74 per \$1USD the fair value of the investment as of May 31, 2008 was \$551mm. In late June KSK completed the IPO at a final price of Rs240 per share, raising \$194mm.

Based on our audit procedures we believe the approach and assumptions used by Lehman to determine the fair value of the investment as of May 31, 2008 were appropriate.

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Europe Volatility - \$170mm in losses from Exotic books clean-up

The Europe Volatility business incurred losses of \$170mm in Q2'08 related to the clean-up of the exotics books. The losses were comprised of the following:

1. \$28mm loss from booking of reserves on Treasure Options
 - a. The original model used to value these trades was deemed inappropriate because it uses a flat volatility. Lehman is currently using its best available models to value the trades. These two stochastic models (OU and VMM models), which are considered most suitable, produced MTM differences of \$42 million. The front office traders contend that the trade has more convexity than the models can capture. As a result, the reserve was lowered to \$28 million to reflect this uncertainty.
2. \$20mm loss from booking of reserves for FX/EQ correlation
 - a. This reserve was booked because Product Control in conjunction with the Front Office identified that the FX/EQ correlations had not been updated during the quarter because the valuation models were using a series of inputs that were not representative of the current market conditions. Based on the use of inputs which reflect current market conditions the Europe Volatility business took a \$20mm reserve. Reserves were taken as of the end of Q2'08 in order to allow the business and Product Control time to further refine the pricing of FX/EQ correlation.
3. \$13mm loss from dividend yield remarks based on refined price testing procedures
4. \$17mm loss from Type 28 deferrals
 - a. Type 28 deferrals are differences in P&L between traders and the desk due to known reasons such as timing of trade bookings and known system errors. There are established rules between traders and Product Control where Type 28 deferrals are tracked and will be reversed once the issues are resolved.
5. \$40mm loss from hedging losses, particularly from mishedging of Treasure Option trades
6. \$30mm loss from Operations booking errors of 10 trades

The business is investigating the causes of the operational issues above in order to minimize such events in the future.

Goodwill and Intangible Assets

The Company's typically tests for impairment of Goodwill and Intangible Assets during the third quarter. Pursuant to FAS 142, Goodwill of a reporting unit shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of a reporting unit below its carrying amount. As a result of market conditions during the second quarter, the Company's stock price was trading below book value. Therefore the Company conducted an impairment test on Goodwill and Other Intangible assets and concluded that no impairment was identified. The following is a break out of the Company's Goodwill and Intangible assets as of May 31, 2008:

Summary Review Memorandum***Bid/Offer Valuation Adjustment***

This adjustment is made at the portfolio level to account for the potential loss from closing out the risk exposure of a parameter at its exit price in its principal market - long (short) exposure at the bid (offer) respectively. The bid-offer adjustment may apply to all market model parameters and related risk exposures such as underlying prices/rates (Delta), volatilities (Vega), and correlations (Correl). A net risk exposure by maturity bucket is calculated for each portfolio for various types of risks (e.g. interest rate, volatility, correlation, etc.). The adjustment is then derived by applying the relevant liquidation costs based on current bid/offer spreads obtained from external broker sources against the net exposure for that particular risk type.

The total \$451 million in bid/offer adjustments, and a net \$10 million decrease in Bid/Offer valuation adjustments is primarily due to a decrease in risk exposure as well as tightening of credit spreads in the High Grade and High Yield (HG/HY) Credit, and Synthetic CDO areas.

Liquidity/Concentration Valuation Adjustment

Product Control maintains a liquidity reserve for less liquid positions or positions having excessive risk on certain specific exposures. Liquidity adjustments are considered an extension of bid/offer adjustments for specific products or markets that are considered to be less liquid or where a concentration of positions makes the current bid/offer spread unobtainable. Liquidity adjustments are needed due to the uncertainty over the ability to transact at observed market levels. These adjustments are needed to value positions at an appropriate exit price.

The total \$136 million in liquidity adjustments, and net \$80 million decrease in liquidity valuation adjustments, is primarily due to the unwinding of trades and the tightening of credit spreads. Further, there was a reduction in the liquidity adjustment for NTD correlation exposures due to change in methodology (change from equity pair-wise correlations to flat correlations) and also due to reclassification of NTD historical correlation reserves to Bid-offer including reduction in recovery reserves driven by tightening credit markets.

Based on our understanding of the risk profile and complexities of these portfolios, we believe the above amounts are reasonable to appropriately reflect the related derivative inventory at fair value.

Model Reserves

Majority of the derivative trades traded by Lehman are over the counter or OTC type trades and are valued using proprietary models. Model reserves are recorded by Lehman due to several reasons across various derivative businesses which includes model limitations to price certain exposure, unapproved or temporarily approved model, long dated trades having input limitations, model calibration limitations etc. All significant model reserves are determined jointly by the Product Controllers, Risk Management, and the trading desk, and reviewed by the Model Control Committee. Periodic reviews of these adjustments are performed to ensure that the appropriate levels of adjustments are maintained.

The total \$297 million in model valuation adjustments, and net \$63 million decrease in model valuation adjustments, is primarily due to decreases in exposure across various businesses resulting in fewer model valuation adjustments.

Based on our understanding of the risk profile and complexities of these portfolios, we believe the above amounts are reasonable to appropriately reflect the related derivative amounts at fair value.

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Reporting Unit	Goodwill	Indefinitely Lived		Intangible Assets (net of amortization)	Total
		Intangible Assets			
Investment Management	\$ 2,253	\$ 519		\$ 341	\$ 3,113
Capital Markets	1,039	-		(51)	988
Investment Banking	-	-		-	-
	<u>\$ 3,292</u>	<u>\$ 519</u>		<u>\$ 290</u>	<u>\$ 4,101</u>

We have inquired with management as to their process on its impairment test and noted that nothing came to our attention that would lead us to believe that impairment existed in 2Q '08.

Reserves, Deferrals, and Valuation Adjustments

As part of our quarterly review procedures, EY auditors performed analytical review procedures on various reserve balances.

Valuation Adjustments

In line with industry practices and to ensure its inventory is appropriately valued in accordance with FAS 157, Lehman Brothers prices its derivative trades using several types of valuation adjustments, including bid/offer, model, liquidity, etc. The table below lists the global fixed income derivatives valuation adjustments by adjustment type across the various product types as of May 30, 2008 and February 29, 2008:

Adjustment Type (in thousands)	Q2 '08	Q1 '08	\$ Variance
Bid/Offer	450,988	\$461,289	(10,031)
Liquidity/ Concentration	136,290	215,855	(79,565)
Model	297,283	360,535	(63,252)
Credit	1,641,921	548,936	1,092,985
Other	134,735	317,867	(183,132)
Total	\$2,661,217	\$1,904,482	\$757,005

The valuation adjustments policy consists primarily of bid/offer, liquidity, model, credit, and other specific valuation adjustments across various product types. The valuation adjustment policy has been consistently applied as compared with prior periods, except where changes in estimations were supported by changes in market factors/industry practice. We obtained support for all valuation adjustment balances and reviewed for reasonableness without material exception. We obtained the general ledger reconciliation performed by Product Control, which compares the requirement versus the general ledger balance, and noted no material exceptions with respect to the legal entity allocation and appropriateness of the amounts recorded on the books and records.

For the significant valuation adjustments listed above, we obtained an understanding of the main components, as well as explanations for large quarter-over-quarter fluctuations:

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Credit

The total \$1.6 billion in credit adjustments, and a net \$1.09 billion increase in credit valuation adjustments is primarily due to counterparty credit adjustments in the CDO Americas business as well as the Municipals' business. Increase is mainly attributable to: 1) increase in MTM on trades with ACA and 2) increase in percentage of MTM needed to cover counterparty risk on trades with XL Capital. Lehman has reserved almost 99% of MTM of all trades with ACA since the counterparty is now classified under Non-performing counterparties category. Regarding XL Capital, the reserve requirements were increased due to ongoing deterioration in the credit condition of XL Capital requiring a larger % of total MTM to be reserved (approximately 52%). Please see CVA section for further details.

Other

The total \$134mm in other valuation adjustments, and a net \$183mm decrease in these adjustments is due to settlement of claims with Peloton and thus valuation adjustments were released. Further, due to the completion of deal reviews, P&L was released on CDO trades in Europe.

As a result of our review performed, the Fixed Income Derivatives valuation adjustments appear reasonable as of Q2.

Legal Reserves

We inquired of internal counsel on significant litigation based on previous discussions and the client's analysis of probable and estimable legal reserves as of May 31, 2008. This inquiry of legal counsel is performed in lieu of a separate legal confirmation.

The total amount booked as NPE Litigation Reserves at May 31, 2008 was approximately \$95mm versus approximately \$93mm at February 29, 2008. The slight increase over the prior quarter-end is attributable to new reserves, changes in current reserve balances and write-offs of old reserves. The addition of the Enron, SEC Auction Rate Inquiry and the Dean Morris reserves increased the NPE Litigation Reserve by \$2mm. Changes as a result of revised estimates in the Analyst Investigation (Joint SRO) and NCRC reserves decreased the NPE Litigation Reserve by \$1mm. Write-offs of the IPO Fee Litigation and the Financial Freedom reserves due to settlement increased the NPE Litigation Reserve by \$1mm. We noted that these changes were not significant individually or in the aggregate.

Based on our review, the legal reserves appear fairly stated at May 31, 2008.

Corporate Valuation Reserves

The total Corporate Valuation Reserve balance at May 31, 2008 was \$103mm compared with \$128.5mm at February 29, 2008. Below is a summary of the significant activity that occurred in this account during the quarter:

- Decrease of \$25mm in the reserve for Marubeni – In prior quarter, \$50mm was reserved for Marubeni as it relates to a complaint filed with the Tokyo District Court, Civil Division, against Marubeni Corporation, seeking a payment of \$351mm due under certain contracts entered into with Marubeni in October and November of 2007. In the current quarter, the

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\$50mm reserve was reversed from Corporate's reserves and reclassified and reserved on Asia's books. In addition, during the second quarter, an additional \$25mm was reserved for the Marubeni complaint based on exposure. Reclassification of reserve to Asia's book and additional reserve recorded amounted to net decrease of \$25mm.

Based on our review, the corporate valuation reserves appear fairly stated at May 31, 2008.

Marubeni Reserve

On March 28, 2008, the Company filed a complaint with the Tokyo District Court, Civil Division, against Marubeni Corporation, ("Marubeni"), seeking payment of \$351 million due under certain contracts entered into with Marubeni in October and November of 2007. Marubeni has repudiated its obligations under those contracts, maintaining that several Marubeni employees forged documents and made misrepresentations to create the impression that Marubeni had committed to the transaction, which involved the financing of various projects and purchases for hospitals and other medical institutions in Japan. The Company has reported the conduct of the Marubeni employees and certain other individuals involved in the transaction, including a former senior officer of Marubeni, to the Tokyo police, who are conducting an investigation into possible criminal fraud.

The Company has reserved approximately \$50 million relating to the Marubeni litigation. The Company has concluded that it has a meritorious claim against Marubeni and that they intend to pursue this case vigorously. The Company believes that it will recover all assets, but would be willing to settle the claim for approximately \$300mm and accordingly has reserved approximately \$50mm.

Taxation Matters

Lehman's effective tax rate for the quarter ended May 31, 2008 was 32.7%% compared to 33.3% for the quarter ended May 31, 2007. The Company's effective tax rate for the six-month period ended May 31, 2008 and 33.3% as compared to 32.4% for the six-month period ended May 31, 2007.

Internal Control Update

In accordance with PCAOB Standard No. 5 we have performed review procedures related to the Company's internal controls over financial reporting. This additional effort included inquiry of senior management as to the functioning of internal controls and changes in the internal control environment, observation of controls in place at July 10, 2008 and review of various key controls. Such areas include:

- Entity Level Controls
- Management Reporting
- External Reporting
- Accounting Policy
- Reserves, including Legal, Credit and Corporate
- Tax
- Securitizations
- Deferrals and Timing
- Valuation Adjustments
- Commissions
- Investment Banking
- Non-Personnel Expenses
- Compensation
- Regulatory
- IT
- Model

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We are not aware of any material modifications that should be made to the disclosures about changes in internal control over financial reporting in order for management's quarterly certifications to be accurate and to comply with the requirements of Section 302 of the Act.

Additionally, Bill Schlich, Coordinating Partner attended the quarterly CEO/CFO Certification meeting held on July 8, 2008. At this meeting all direct reports to the CEO affirmed there are no significant control related matters in their areas. Bill Schlich and Art Tully also attended the Company's April 2, 2008, May 7, 2008, and June 13, 2008 Audit Committee meetings. No significant items were noted.

At the CEO/CFO Certification meeting and the Audit Committee meeting, we reviewed the quarterly results and review procedures performed.

Other

On June 30, 2008, key members of the engagement team met to discuss comments on the Company's 10Q filing and preliminary results of our review procedures. The following individuals participated:

- Bill Schlich, Coordinating Partner
- Paul Haus, Independent Review Partner
- Joe Link, Partner- Corporate- Corporate
- Stavros Zafiridis, Manager- Corporate
- Jerry Gruner, Senior Manager- Mortgage Capital
- Jennifer Jackson, Senior Manager- Derivatives
- Bharat Jain, Manager- Derivatives
- Alex Gironde- Senior Manager- Equities

Independence Update

In conjunction with our quarterly review of the Company we completed the U602A, Program for Annual Public Company Independence Procedures – Update. As such we performed the following steps:

1. Inquired of Martin Kelly, Lehman Managing Director re: any changes in the Company's organizational structure. A list of new entities was obtained from the Lehman Consolidations Group and updated in the Family Tree Validator in the Global Independence System.
2. Inquired of Martin Kelly regarding any new employment relationships at the Company related to alumni of E&Y in accounting or financial reporting roles, individuals who had previously not been in an accounting or financial reporting role who changed positing or if any offers of employment were made to engagement team members or their families. No new employment relationships to note at Lehman - refer to PCIP procedures for additional discussion.

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3. Inquired of Martin Kelly regarding any new business relationships between Lehman and its affiliates and E&Y and its affiliates. No items were noted.
4. Reviewed new engagements and current audit committee pre-approvals. All services appear in accordance with SEC rules and Audit Committee pre-approvals.

Based on the procedures described above, we continue to believe we are independent of the Company.

Conclusion

Based on our review of Company's unaudited interim consolidated financial statements as of and for the three and six-month periods ended May 31, 2008, nothing came to our attention that indicates that a material modification should be made to the unaudited interim financial statements in order for them to be in conformity with U.S generally accepted accounting principles.

Furthermore, we are not aware of any material modifications that in our judgment should be made to the disclosures about changes in internal control over financial reporting in order for management certification to be accurate and to comply with the requirements of Section 302 of the Sarbanes-Oxley Act of 2002.