

February 10, 2009

Research Update:

**Customer Asset Protection Co.
Downgraded To 'B-'; Ratings To Be
Withdrawn**

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Rationale

On Feb. 10, 2009, Standard & Poor's Ratings Services lowered its counterparty credit and financial strength ratings on Customer Asset Protection Co. (CAPCO) to 'B-' from 'BB'. At the same time, we removed the ratings from CreditWatch, where they had been placed with negative implications on Sept. 16, 2008. The outlook is negative. Subsequently, we will withdraw the ratings at the company's request.

The downgrade reflects Standard & Poor's assessment of CAPCO's potential liability to clients of Lehman Brothers International (Europe) (LBIE). Although there is still tremendous uncertainty surrounding the administration of LBIE, Standard & Poor's believes the situation could create a liability for CAPCO that exceeds the insurer's resources.

Our primary concern regarding CAPCO clearly is the potential for a claim related to the clients of LBIE that opted to rehypothecate their assets to LBIE. Rehypothecation is the practice of a client allowing its broker/dealer to pledge the client's assets as collateral for the broker/dealer's loans. The administrator in the liquidation of LBIE has stated that most of the clients who rehypothecated their assets will rank *pari passu* with the broker/dealer's general creditor. If LBIE's liabilities exceed its assets, the administrator will assign a percentage of that loss to the pool, and this loss will be allocated by account size. The pool will also bear the broker/dealer's cost of distributing the remaining assets to the pool.

CAPCO's claims-paying resources are modest relative to the size of the general creditors' pool; therefore, allocating even a small percentage loss to the pool could cause problems for CAPCO. CAPCO's liability for clients who permitted their assets to be rehypothecated is unclear. The company's policy neither explicitly covers nor excludes losses arising from the rehypothecation of assets. CAPCO's claims-paying resources include its own investment portfolio, which consists mostly of short-term obligations of the U.S. government and reinsurance coverage from financial guarantors. In the event of a sizable claim, CAPCO would benefit from approximately \$200 million of reinsurance from two reinsurers.

Standard & Poor's does not expect CAPCO to incur a significant liability from insuring LBIE's other client accounts. At a meeting of general creditors in November 2008, the administrator said that all client assets will be returned to their owners. We believe the administrator of the liquidation has segregated these clients' assets and has already transferred some assets to other brokers. These clients may still face long delays in obtaining access to their assets, but CAPCO's insurance does not reimburse clients for a decline in the market value of their securities or adverse circumstances that may arise from being unable to access or trade their securities.

Standard & Poor's does not believe CAPCO's insurance for members other

than LBIE will result in a claim. None of CAPCO's members elected to renew their policies. Consequently, the company's coverage will expire on Feb. 15, 2009. A U.S. member cannot file a claim unless the Securities Investor Protection Corp. (SIPC) initiates a liquidation proceeding while its policy is in force. In the U.K., an event is eligible for coverage if the broker/dealer files for bankruptcy or is placed in administration. At this time, Lehman Brothers Inc. (Lehman U.S.) is the only member that could file a claim. SIPC has initiated a liquidation proceeding for Lehman U.S., but there has been no indication that clients' funds were misappropriated. Many accounts already have been transferred to other broker/dealers.

Ratings List

Downgraded; CreditWatch/Outlook Action

	To	From
Customer Asset Protection Co.		
Counterparty Credit Rating		
Local Currency	B-/Negative/--	BB/Watch Neg/--
Financial Strength Rating		
Local Currency	B-/Negative/--	BB/Watch Neg/--

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