Transaction Advisory Services

Project LLC : Summary of Findings and Observations Report

June 26, 2008

Reliance Restricted

Ernst & Young

Quality In Everything We Do

Ernst & Young LLP
5 Times Square
New York, NY 10036

June 26, 2008

Reliance Restricted

Ms. Helen Mucciolo
Senior Vice President
Federal Reserve Bank of New York
33 Liberty Street
New York, NY 10045

Dear Ms. Mucciolo:

At the Federal Reserve Bank of New York's ("FRBNY") request and direction, we performed certain due diligence procedures in connection with the FRBNY's financing to Maiden Lane LLC as it relates to JPMorgan Chase & Co.'s ("JPMorgan") acquisition of Bear Stearns Companies Inc. ("Bear Stearns"). The procedures performed by us are included in the *Due diligence procedures performed* section of the report. Any differences between the procedures set forth in this report and those set forth in our engagement letter reflect modifications that were made at your request or discussed with you during the course of the engagement.

The procedures that we performed do not constitute an audit of Bear Stearns' historical financial statements in accordance with generally accepted auditing standards, nor do they constitute an examination of prospective financial statements in accordance with standards established by the American Institute of Certified Public Accountants. Additionally, the procedures do not address the effectiveness of internal controls over financial reporting under Section 404 of the Sarbanes-Oxley Act. Also, except for ascertaining that certain information in tabulations and reports received from Bear Stearns agreed with the accounting records (as specifically identified in the accompanying memoranda, summaries and schedules), we performed no procedures to evaluate the reliability or completeness of the information obtained. Accordingly, we express no opinion or any other form of assurance on the historical or prospective financial statements, management representations or other data of Bear Stearns included in or underlying the accompanying information. While we believe the information obtained is substantially responsive to your request, we are not in a position to assess its sufficiency for your purposes. In addition, we have no responsibility to update this report for events or circumstances occurring after the date of this report.

In performing the due diligence procedures, we have accumulated data, written various memoranda for our own use and the use of other members of the due diligence team, and have had various meetings with representatives of the FRBNY, BlackRock Financial Management, Inc., JPMorgan and Bear Stearns. The procedures performed and related findings are presented in the attached *Transaction Insights* which are attached for your use.

This report is intended for use solely by members of the FRBNY's management, its Board of Directors and its legal advisors. Copies should not be made, nor should this report be distributed to others without our express permission.

Very truly yours,

Ernst + Young LLP

Abbreviations

ABS	Asset-backed mortgage securities
ABX	Asset-backed mortgage securities index
ADP	BS' general ledger system
Negotiated value	Value of assets and hedges based on prices negotiated between BLK and JPM
AICPA	American Institute of Certified Public Accountants
ARM	Adjustable rate mortgage
BITS	Back-office profit and loss system for foreign equity and fixed income securities
BLK	BlackRock Financial Management, Inc. (asset manager and advisor to the FRBNY)
BO	Back-office
BofA	Bank of America
BS or BSC or Bear Stearns	The Bear Stearns Companies Inc.
BSCMI	Bear Stearns Commercial Mortgage, Inc.
BTS	Back-office profit and loss system for equities, macro hedges, and municipal securities
BUC	Business unit controller
CDO	Collateralized debt obligation
CDS	Credit default swap
CLO	Collateralized loan obligation
CMO	Collateralized mortgage obligation
CMBS	Commercial mortgage-backed securities
CMBX	Commercial mortgage-backed mortgage securities index
CurBal	Current balance of commercial and residential mortgage loan
Carrying value or CV	Value of assets and hedges based on marks or prices in BS' books and records at March 14, 2008 as well as value of assets and hedges where the marks or prices used were negotiated and agreed to by the FRBNY, BLK and JPM
CVA	Credit valuation adjustment

Abbreviations

DTC	Depository Trust Company
DTCC	Depository Trust & Clearing Corporation
DVP	Deliver vs. payment
Eligible	Refers to the portfolio acquired by the LLC in accordance with established demarcation guidelines
EMC	EMC Mortgage Corporation, a mortgage servicing subsidiary of BS
EOD	End of day
EY	Ernst & Young LLP
FAST group	BS' Financial Analytics and Structured Transactions Group
FIPR	BS' securities master
FICO score	Fair Isaac Corporation (credit score)
FITE	BS' operation desktop front office system
FNMA	Fannie Mae (Federal National Mortgage Association)
FO	Front office
FRBNY	Federal Reserve Bank of New York
GIC	Guaranteed investment contract
GMAC	GMAC Mortgage
GOTS	Back-office profit and loss system for mortgage securities
GOVT or GOVTRDR	Middle-office profit and loss system for U.S. Treasuries
GSE	Government sponsored enterprise
HELOC	Home equity line of credit
IAN	Indexed amortizing note
IC	Interest coverage
IDC	Interactive Data Corp.
IO	Interest-only
IOPS	Back-office profit and loss system for equities, corporate bonds, asset-backed mortgage securities, and

Abbreviations

	Euroclear securities
IRS	Interest rate swap
ISDA	International Swaps and Derivatives Association, Inc.
ITG	Information Technology Group of BS
JABBA	BS' commercial loan system
JPM	JPMorgan Chase & Co.
LIBOR	London Interbank Offered Rate
LLC	Maiden Lane LLC
LTV	Loan to value
MBS	Mortgage-backed securities
MORT or MORTTRDR	Middle-office system for mortgage-backed mortgage securities
MRS	Management reporting system
MSRs	Mortgage servicing rights
MTM	Mark to market
OC	Over collateralization
P&I	Principal and interest
P&L	Profit and loss
PiWorks	Servicing system for commercial mortgage loans
PAUG	Pay as you go
PB2	BS' daily market value system
PRISM	BS' risk management system for mortgage securities
Proteus/Poseiden	Front office system for credit derivatives
Resi	Residential mortgage loans
REO	Real Estate Owned
Refob	Reference obligation

Abbreviations

Repo	Repurchase agreement
Reverse repo	Reverse repurchase agreement
RM	Risk management
S&D	Scratch and dent
S&P	Standard and Poor's
SBA	Small business administration
SBO 2000	Back-office system for residential mortgage loans
SFAS	Statement of Financial Accounting Standards
SOD	Start of day
SPV	Special purpose vehicle
Summit	Front office system for interest rate derivatives
SWAP/Derivclear	Back-office system for credit and interest rate derivatives
TABX	Tranche ABX
TBA	To be announced
Tiger2	BS' ticketing system for derivatives
TRS	Total return swap
UniFi	BS' front office system for originated loans
UPB	Unpaid principal balance
USD	U.S. dollar
WITS	Whole loan inventory tracking system, a back-office system for residential mortgage loans

Contents

Transaction Insights

Transaction overview

Transaction overview

On March 28, 2008, The Federal Reserve Bank of New York ("FRBNY") and JPMorgan Chase & Co. ("JPM") entered into an arrangement related to the financing provided by the FRBNY in connection with JPM's acquisition of the Bear Stearns Companies Inc. ("BS") ("Term Sheet"). Under this arrangement, a Delaware limited liability company, Maiden Lane LLC (the "LLC"), with the FRBNY as its sole Managing Member, acquired from BS a pre-defined portfolio comprised of assets and hedges for a cash purchase price aggregating $29.97 billion. The assets and the related hedges were identified by JPM, the FRBNY, and BlackRock Financial Management, Inc. ("BLK") (in its capacity as the asset manager and advisor to the FRBNY) in accordance with established guidelines agreed upon by the parties. To facilitate the acquisition of the portfolio by the LLC, the FRBNY extended an approximately $28.82 billion loan and JPM extended a $1.15 billion loan to the LLC. The transaction closed on June 26, 2008.

The following table presents a summary of eligible assets and hedges included in the transaction:

Eligible assets and hedges

Currency: $millions	Notes	Carrying value	Accrued interest	Net purchase price
Eligible assets	1	26,529.8	113.1	26,642.9
Non-credit hedges	2	18.0	-	18.0
Credit and interest rate derivatives	3	3,332 3	(0 3)	3,332.0
Top-side adjustments				(23.3)
Total eligible assets and hedges acquired by the LLC		**29,880.1**	**112.8**	**29,969.5**
Source of funding:				
FRBNY loan				28,819.5
JPM loan				1,150.0
				29,969.5

Source: Transaction Foundations Databook
Ref: Eligible assets and hedges and pre-closing date proceeds - Section Lead - Lead Schedules

1 Include mortgage securities, commercial mortgage loans and residential mortgage loans.
2 Include equity options and options on Futures.
3 Include interest rate swaps, single name credit default swaps and CMBX.

ERNST & YOUNG

Transaction overview

The LLC also acquired other non-credit hedges including Eurodollar and Treasury futures, TBAs, U.S. Treasuries, and equity shorts for which the LLC/FRBNY did not pay a specific cash purchase price at closing and as a result required no additional funding by the FRBNY. For U.S. Treasuries, the transfer to the LLC was carried out via a repurchase and reverse repurchase agreement (see *Repurchase and reverse repurchase agreements* for further discussion). For other non-credit hedges that had no transfer values at closing, a net realized P&L settlement will occur post-close.

Carrying values of assets and hedges

The carrying values of eligible assets and hedges included in the LLC portfolio acquired (i.e., purchase price paid by the LLC) were generally based on the marks or prices of such assets and hedges on the books of BS as of March 14, 2008 irrespective of any mark-downs or mark-ups on the assets and hedges relating to changes in value after March 14, 2008, except as follows:

- Certain mortgage securities were not on the books of BS at March 14, 2008, as these were held in unconsolidated SPVs. These securities were brought back on to the balance sheet of BS subsequent to March 14, 2008 and included in the eligible portfolio. The value of such securities was based on marks or prices negotiated between BLK, in consultation with the FRBNY, and JPM. These securities had no March 14, 2008 prices on the books of BS since these were only subsequently recorded/consolidated into BS' mortgage securities inventory after March 14, 2008 (see further discussion in the *Executive summary* section).
- CMBX positions were based on "Mark-It Partners" prices as of March 14, 2008, as negotiated between BLK, in consultation with the FRBNY, and JPM.

It is likely that the value of these eligible assets and hedges recorded by the LLC at closing were different from the values noted above, as the market prices have moved between March 14, 2008 and June 26, 2008.

Total return swaps

At closing, the LLC and JPM entered into a Total Return Swap ("TRS") with respect to the credit default (""CDS") and interest rate swap ("IRS") transactions included in the transaction. The LLC made an initial payment to JPM in the aggregate amount of $3.3 billion, which is included in the purchase price (see table presented on page 3). Under the TRS, the LLC and JPM are deemed to have entered into mirror CDS and IRS transactions with terms identical to the terms of the underlying CDS and IRS transactions. The TRS was designed such that the LLC's economic position under each mirror transaction replicates the economic position of BS under the corresponding CDS or IRS transaction.

ERNST & YOUNG

FCIC-ML0000011

Highly Confidential

Transaction overview

CMBX

As indicated in section 2 (c) of the TRS, the identified eligible CMBX transactions were to be combined into 26 CMBX transactions, each of which were separately confirmed between JPM and the LLC and were deemed to be mirror transactions under the TRS.

Repurchase and reverse repurchase agreements

In connection with the transfer of the long and short positions of eligible U.S. Treasury securities with an aggregate net carrying value of $5.9 billion, the LLC entered into repurchase ("repo") and reverse repurchase agreements ("reverse repo") with JPMorgan Securities Inc. ("JPMSI"). At closing, the transfer of the U.S. Treasuries to the LLC was carried out as follows:

- Repo: BS delivered the long U.S. Treasury securities with an aggregate carrying value of $6.7 billion to the LLC at no specific purchase price (i.e., included at no cost). The LLC then entered into repo arrangements with JPMSI delivering the U.S. Treasury securities and receiving $6.7 billion, which the LLC paid to BS to settle the purchase of the U.S. Treasury securities.
- Reverse repo: JPMSI sold to the LLC U.S. Treasury securities settled via "deliver vs. payment" or DVP. The LLC then entered into reverse repo arrangements delivering the U.S. Treasury securities to BS and receiving cash for $872 million, which the LLC paid to JPMSI to settle the purchase of the U.S. Treasury securities.

Pre-closing date proceeds

In addition to the acquisition of the collateral pool by the LLC, the LLC was entitled to pre-closing date proceeds, which represent amounts paid or received (or expected to be paid or received, as applicable) with respect to the assets and hedges included in the collateral pool during the period from and including March 14, 2008 to June 26, 2008 ("closing date"). The pre-closing date proceeds include:

- scheduled repayments or prepayments of principal and interest ("P&I") or other yield payments received on the collateral pool; plus
- the cash proceeds from the sale, assignment, transfer or disposition of assets and hedges included in the collateral pool; minus
- allocated funding costs calculated at the Primary Credit Rate (i.e., cost of carry) net of reinvestment earnings credit calculated at the same Primary Credit Rate.

Transaction overview

At closing, the LLC received net cash flows aggregating $606.2 million, which represents the initial pre-closing date proceeds during the period from March 14, 2008 to cut-off date applicable for each asset class as agreed among the FRBNY, BLK and JPM as follows:

Assets / Hedges	Cut-off date for P&I cash flows	Cut-off date for sales proceeds
Mortgage securities	May 16, 2008	May 22, 2008
Commercial mortgage loans	May 31, 2008	May 31, 2008
Residential mortgage loans	April 30, 2008	n/a (no sales)
U.S. Treasuries	May 16, 2008	n/a (no sales)
Credit and other non-credit hedges	n/a (all pre-closing date proceeds will be determined post-close)	n/a (all pre-closing date proceeds will be determined post-close)

The pre-closing date proceeds from cut-off date to June 26, 2008, along with reinvestment earnings credit calculated at the Primary Credit Rate, will be paid to the LLC post-close. In addition, a true up of any adjustments to the initial pre-closing date proceeds settled at closing will occur post-close.

Trust and master servicing agreements

Maiden Lane Commercial Mortgage-Backed Mortgage securities Trust 2008-1 ("Trust Fund")

In connection with the transfer to the LLC of the trust certificate related to the eligible commercial mortgage loans, Bear Stearns Commercial Mortgage, Inc. ("BSCMI") as depositor, U.S. Bank National Association, as trustee, and Bank of America, N.A., as master servicer entered into a trust and servicing agreement dated as of June 26, 2008.

Maiden Lane Asset Backed Mortgage securities I Trust 2008-1 ("Trust Fund I")

In connection with the transfer to the LLC of the trust certificate related to the eligible residential mortgage loans, EMC Mortgage Corporation, as depositor, U.S. Bank National Association, as trustee, and Wells Fargo Bank, N.A., as master servicer and mortgage securities administrator entered into a trust and servicing agreement dated as of June 25, 2008.

Scope

The scope of our work has been determined by the FRBNY. The specific procedures performed are listed in the *Due diligence procedures performed* section of the report. Any differences between the procedures set forth in this report and those set forth in the engagement letter reflect modifications that were requested by or discussed with the FRBNY during the course of the engagement.

Transaction overview

The procedures we performed were designed to focus on financial and transaction risks identified by the FRBNY associated with the assets and hedges included in the collateral pool with emphasis on the following:

- identification of eligible assets and hedges in accordance with established guidelines;
- understanding the process flows and the reconciliation of data with BS' books and records for each of the asset classes;
- obtaining supporting internal or external documentation for eligible assets and hedges;
- obtaining documentation and discussion with BS management related to marks or prices of eligible assets and hedges; and
- identification of cash flows related to eligible assets and hedges from March 14, 2008 to closing date, June 26, 2008.

Our work primarily consisted of (i) analysis of information provided by BS and obtained from external sources, and (ii) discussions with members of BS, JPM, BLK and the FRBNY.

Limitations in scope

Our engagement was limited to the due diligence procedures listed in the *Due diligence procedures performed* section of this report, and accordingly we did not address matters that may be addressed by the FRBNY directly, or by their other advisors. Specifically, and among other matters, we did not perform any services with respect to:

- financial and accounting due diligence;
- credit and portfolio analysis;
- litigation, compliance or regulatory risks;
- contract and other corporate legal matters, including any potential change of control provisions;
- valuation;
- insurance matters;
- human resource matters;
- IT hardware, security and other areas.

Transaction overview

This report may not encompass all the schedules or materials received from BS or JPM, or verbal or written comments previously made to the FRBNY. The comments and observations in this report are focused principally on those matters that, based on discussion with the FRBNY, we believe could be of significance or interest to the FRBNY or might require further consideration. Other factors beyond the scope of this engagement should be considered by the FRBNY in evaluating all of the merits/risks of the proposed transaction, including, but not limited to, inherent business, financial, legal, operations, technology, risk management, regulatory and other transaction risks.

The amounts presented in tables and charts were rounded to the nearest million or thousand unless otherwise specified. Certain analyses may have differences in footing due to rounding.

The number or count of items presented in tables and charts were based on unique identification numbers such as CUSIP, loan ID and client ID unless otherwise specified.

Executive summary

Purchase price of eligible assets and hedges

Calculation of "trim" amount

Currency: $millions	Note	
Assets identified during the demarcation process:		
Mortgage securities		16,858.3
Commercial mortgage loans		8,230.9
Residential mortgage loans		1,604.6
Total cash assets		26,693.7
Less: Non-credit hedges		
Interest rate derivatives		(334.5)
Equity options		(3.4)
Option on Futures		21.4
		(316.5)
Net cash assets		26,377.2
Target amount of cash assets determined by BLK, FRBNY and JPM	1	26,330.6
Amount to be trimmed		**46.6**
Add back: 11 loans with missing documents removed previously		0.7
Original "trim" amount		47.4
Allocation of total amount to be trimmed between residential mortgage loans and mortgage securities:		
Residential mortgage loans (50% of original trim amount)		23.7
Less: 11 loans with missing documents		0.7
Remaining residential mortgage loans to be trimmed		23.0
Mortgage securities (50% of original trim amount)		23.7
Total amount to be trimmed		**46.6**
Actual amount trimmed		**46.8**
Difference		**(0.2)**

Source: Final Demarcation Totals 06-19-08 6am.xls (BLK)

Ref: Calculation of amount to be "trimmed" - Section Lead - Lead Schedules

1 The Term Sheet between the FRBNY and JPM had an original target of $26.3 billion of cash assets and $3.7 billion of derivatives. However, as a result of 16 CDS that were removed due to confirmation issues (see Appendix A for the demarcation guidelines provided by BLK) aggregating to $30 million, it was agreed among the FRBNY, BLK and JPM to reduce the target for derivatives by $30 million to $3.67 billion and increase the target for cash assets to $26.33 billion.

Note: Footing differences are due to rounding.

Demarcation guidelines

As discussed in the *Transaction overview* section, the eligible assets and hedges were identified in accordance with established guidelines agreed to by the FRBNY, BLK and JPM (see Appendix A for the demarcation guidelines provided by BLK). In addition, the identification of certain eligible hedges was negotiated between BLK, in consultation with the FRBNY, and JPM. Following the demarcation process, the identified eligible assets (net of certain non-credit hedges) aggregated $26.4 billion, which exceeded the targeted value of net eligible assets of $26.3 billion. Therefore, a "trimming" methodology was developed by BLK, in consultation with the FRBNY, and JPM (see table to the left). The actual amount trimmed totalled $46.8 million, which was divided between mortgage securities and residential mortgage loans in the amount of $23.7 million and $23.1 million, respectively, using the following methodology:

After determining the aggregate amount to be "trimmed," the eligible mortgage securities and residential mortgage loans were trimmed based on the following methodology:

- 50% of carrying value (including accrued interest) less the total carrying value of 11 loans with missing documents previously removed was trimmed from the eligible residential mortgage loans.
  - Removed residential mortgage loans serviced by GMAC.
  - Determined the proportion of carrying value (including accrued interest) of first liens vs. second liens in the residential mortgage loans serviced by EMC. The loans were trimmed or removed from the first and second liens in the same proportion. Half of the carrying value was trimmed from the largest loans and the second half was trimmed from the smallest loans.
  - The ratio of carrying value (including accrued interest) for first vs. second liens was rounded to the nearest 0.001%.
  - For each sub-set (e.g., largest 1st lien), the "trim" amount had to meet or exceed the target amount (i.e., take the next loan to push the amount over the target amount).
- 50% of carrying value (including accrued interest) was trimmed from non-agency IOs by taking a proportional reduction in value of all non-agency IOs with a carrying value greater than $10 million.

Purchase price of eligible assets and hedges

Identified eligible assets and related hedges

The table below presents the purchase price for identified eligible assets and hedges as of March 14, 2008 based upon the demarcation guidelines and trimming methodology agreed to by the FRBNY, BLK and JPM:

Eligible assets and hedges

Currency: $millions	Final count	Carrying value and accrued interest before trimming	Trimming of assets	Pre-closing adjustments	Final purchase price
Mortgage securities	2,355	16,858.3	(23.7)	(0.3)	16,834.3
Commercial mortgage loans	137	8,230.9	-	-	8,230.9
Residential mortgage loans	10,986	1,604.6	(23.1)	(3.7)	1,577.7
Total cash assets	**13,478**	**26,693.7**	**(46.8)**	**(4.0)**	**26,642.9**
Non-credit hedges	16	18.0	-	-	18.0
Credit and interest rate derivatives	4,567	3,335	-	(3)	3,332
Total before top-side adjustments	**18,061**	**30,046.7**	**(46.8)**	**(7.0)**	**29,992.8**
Top-side adjustments:					
Matched ARMs book					(16.7)
CVA					(6.6)
Total purchase price					**29,969.5**
Less: JPM's funding commitment					1,150.0
FRBNY's funding commitment					**28,819.5**

Source: Transaction Foundations Databook
Ref: Summary of eligible assets and hedges - Section Lead - Lead Schedules

Purchase price considerations

Based on our understanding, prior to closing on June 26, 2008, the FRBNY re-negotiated the terms of the transaction with JPM, which increased JPM's funding commitment from $1 billion to $1.15 billion, and certain top-side adjustments were made to the total purchase price in light of the following items:

Remark of commercial mortgage loans

- Based on the analysis of daily P&L associated with the commercial securitization conduit loans and correlated hedges from February 29, 2008 to March 20, 2008 and the discussions with BS management of its valuation process, it was noted that on March 15, 2008 and March 16, 2008, BS remarked its commercial mortgage loan portfolio resulting in an approximately $150 million net increase in the carrying value of the eligible commercial mortgage portfolio as of March 14, 2008.

Please see a more detailed discussion in the *Marks analysis – Commercial mortgage loans* section.

Purchase price of eligible assets and hedges

Allocation of CDS remark

Currency: $000	Comparison of 3/14 file with MRS adj	% of IG and Non-IG trades	Impact on eligible CDS
Carrying value amendments to the 3/14 derivatives file	49,388		
MRS adjustments with carrying value impact	156,612		
Difference	**107,224**		
Allocation of the difference to Fed-eligible trades performed by BS:			
Fed IG trades Selected	78,586	100.00%	78,586
Fed Non-IG trades selected	17,406	40.00%	6,962
Trades to be retained by JPM	2,156		
Unallocated	9,077		
Total	**107,224**		**85,548**

Source: Allocation of CDS diff.xls (Pat O'Brien, 6/11/2008)
Ref: Allocation of CDS remark - Section Lead - Lead Schedules

Remark of credit derivatives

- BS management has represented that, in April 2008, the credit derivatives portfolio was remarked due to an incorrect allocation of carrying values to individual trades in the original March 14, 2008 carrying value. Instead of correcting the allocation, BS management remarked certain portfolios using new information, which resulted in a net increase in the value of the credit derivatives portfolio aggregating approximately $107.2 million (including the impact of other MRS adjustments). Of this increase in the value of credit derivatives portfolio, $85.5 million relates to eligible credit derivatives positions (see table to the left).

  Please see a more detailed discussion in the *MRS adjustments* section.

- A portion of the mark up resulted in a purchase price reduction (see Matched ARMs book discussion below). We understand that the remaining differences identified in the credit derivatives remark were considered in the re-negotiation of the deal terms with JPM.

Matched ARMs book

- BS identified seven mortgage security positions that were included in the eligible mortgage securities, which needed to be marked down to offset a portion of the $85.5 million mark up in eligible credit derivatives that was noted above. The aggregate markdown reduced the value by $16.7 million.

Credit valuation adjustment ("CVA")

- The purchase price was reduced by $6.6 million for a credit valuation adjustment to account for the counterparty risk related to the credit derivatives acquired by the LLC.
- The CVA was calculated by allocating the credit valuation adjustment as of February 29, 2008 for the entire population of the BS portfolio to each trade in the eligible portfolio based on a pre-existing weighted average methodology utilized by BS (adjusted for 40% of the CVA related to non-investment grade underlying reference obligations).

Please see a more detailed discussion in the *Marks analysis – Derivatives* section.

Purchase price of eligible assets and hedges

Securities adjustments

- The eligible mortgage securities were largely identified from BS' March 14, 2008 securities inventory. However, certain mortgage securities held by BS in unconsolidated off-balance sheet SPVs at March 14, 2008, with a carrying value of approximately $3 billion, were brought back on to the balance sheet of BS subsequent to March 14, 2008 and were included in the population from which eligible mortgage securities were identified based on the established guidelines.
- The eligible mortgage securities identified from the securities adjustments included 37 mortgage securities referred to as "Liberty Hampshire" portfolio in the books of BS. BS management indicated that these securities were sold to an off-balance sheet SPV in September 2007 in order to get balance sheet relief. However, due to the circumstances around March 14, 2008, an option to put the securities back to BS contained in the agreement with the SPV was exercised. As a result, these mortgage securities reverted back to BS' balance sheet after March 14, 2008.
- As noted in the *Transaction overview* section, the value of these securities held in unconsolidated SPVs at March 14, 2008 was based on marks or prices negotiated between BLK, in consultation with the FRBNY, and JPM. These securities had no March 14, 2008 prices on the books of BS since these were only subsequently recorded/consolidated into BS' mortgage securities inventory after March 14, 2008.
- In April 2008, BS' management has represented that it had recorded MRS adjustments related to Liberty Hampshire positions. These MRS adjustments were considered in the negotiated value of the Liberty Hampshire positions, which reduced the carrying value of identified eligible mortgage securities by $31.9 million from the carrying value reported at March 31, 2008 of $109.4 million to $77.5 million.

Pre-closing adjustments

The following adjustments were made prior to closing:

Mortgage securities

- The following mortgage securities were adjusted prior to closing:

Mortgage securities – pre-closing adjustments

Currency: $000	Carrying value at 3/14	Accrued interest at 3/14	Initial purchase price calculation	Pre-closing adjustment	Adjusted purchase price
90331HLG6	9,672.4	20.0	9,692.4	(178.7)	9,513.7
073868AB7	13,394.3	29.6	13,423 9	(115.9)	13,308.0
Pre-closing adjustment				**(294.6)**	

Source: EY demarcation files
Ref: Mortgage securities - pre-closing adjustments - Section Lead - Lead Schedules

ERNST & YOUNG

Purchase price of eligible assets and hedges

  - One security relates to a corporate bond, which had 2 factors and accrual periods on Bloomberg. The carrying value for this bond was based on the factor and accrual period in the mortgage key as agreed among the FRBNY, BLK and JPM. A true up would appear to be needed post-close once the appropriate factor and accrual period is determined and confirmed with Bloomberg.
  - The original face of a security at March 14, 2008 was noted to be overstated by $227 thousand when compared to the balances reported by the custodian. The value of eligible securities was reduced by $116 thousand to account for the adjustment to the original face to match the original face of the security that was delivered by the custodian to the LLC at closing.
- The accrued interest included in the purchase price of mortgage securities was calculated based on expected cash flows. The FRBNY, BLK and JPM agreed that a true up of expected vs. actual cash flows related to accrued interest will be made post-close to account for any shortfalls in actual cash flows.

Residential mortgage loans

- The FRBNY, BLK and JPM agreed that 32 eligible residential mortgage loans with an aggregate value of $3.7 million were removed from the portfolio just prior to closing due to documentation deficiencies reported by the custodian. Such deficiencies included missing copies of notes and missing or incorrect endorsement on the note.

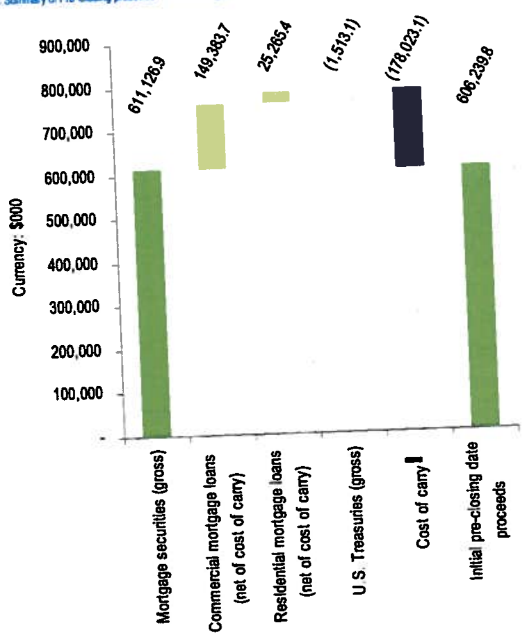
Derivatives

- The portfolio of single name CDS transferred to the LLC was reduced by $3 million as a result of the removal of one duplicate trade, and updated carrying values on 19 trades (15 due to updates to the underlying curves used to determine the carrying value, and four due to the correction of overstated notionals due to assignments).
- At closing, there were potential adjustments identified in the eligible credit derivatives resulting from position or notional differences that have not been fully quantified. As agreed among the FRBNY, BLK and JPM, these will be reconciled and trued up post-close.

Pre-closing date proceeds

Estimated initial pre-closing date proceeds

Source: Summary of Pre-Closing proceeds reconciliation_v4.xls



[1] Cost of carry includes cost of carry on the purchase price net of reinvestment earnings credit related to mortgage securities and U.S. Treasuries cash flows. This amount excludes cost of carry on purchase price of commercial and residential mortgage loans already netted against the cash flows from commercial and residential mortgage loans.

Estimated pre-closing date proceeds

As discussed in the *Transaction overview* section, the LLC is entitled to the pre-closing date proceeds from eligible assets and hedges for the period from March 14, 2008 to closing date of the transaction (i.e., June 26, 2008). The settlement of the pre-closing date proceeds were divided into two payments: (i) the initial pre-closing date proceeds from March 14, 2008 to cut-off dates, as identified in the table below, were paid to the LLC as part of the closing process on June 26, 2008, and (ii) the subsequent pre-closing date proceeds from cut-off dates to June 26, 2008 will be paid to the LLC on a date that will be determined post-close. The cash flows or amounts to be paid to the LLC will include reinvestment earnings credit calculated using the Primary Credit Rate until the date these pre-closing date proceeds are remitted to the LLC.

The chart to the left presents the initial pre-closing date proceeds aggregating $606.2 million, which were remitted to the LLC at closing.

Guidelines observed in estimating the cash flows from eligible assets and hedges

- Based on the guidance received from BLK and the FRBNY on the pre-closing date proceeds, the following guidelines and cut-off dates were observed in determining or estimating the cash flows associated with certain eligible assets and hedges:

Guidelines and cut-off dates for pre-closing and post-closing cash flows

Assets / Hedges	Cut-off date for P&I cash flows	Cut-off date for sales proceeds
Mortgage securities	May 16, 2008	May 22, 2008
Commercial mortgage loans	May 31, 2008	May 31, 2008
Residential mortgage loans	April 30, 2008	n/a (no sales)
U.S. Treasuries	May 16, 2008	n/a (no sales)
Credit and other non-credit hedges	n/a (all pre-closing date proceeds will be determined post-close)	n/a (all pre-closing date proceeds will be determined post-close)

- The estimated cash flows were generally reconciled with BLK and BS. Any individual differences in the estimated cash flows as noted by EY, BLK and BS greater than $1,000 (actual dollars) were investigated and resolved with BLK and BS while differences below $1,000 (actual dollars) were not investigated (as agreed to with the FRBNY). There were net differences which were not investigated aggregating to less than $6 thousand with BS and less than $14 thousand with BLK.

Methodology used in calculating estimated funding costs

- As discussed in the *Transaction overview* section, the pre-closing date proceeds include allocated funding costs associated with holding the eligible assets and hedges in BS' balance sheet prior to closing. The funding cost or cost of carry to be paid by the LLC will be net of reinvestment earnings credit for any cash flows from the eligible assets and hedges received by BS prior to closing. The

Pre-closing date proceeds

following generally describes the methodology for the calculation of funding cost and reinvestment earnings credit agreed to by the FRBNY, BLK and JPM:

1. The LLC will be charged interest on the purchase price (i.e., up to $30 billion) using the daily Primary Credit Rate in effect from March 14, 2008 to the closing date.
2. The LLC will receive interest or reinvestment earnings credit on any payments (e.g., P&I, approved sales proceeds) received from the date payment is received to the closing date at the same Primary Credit Rate.
3. The LLC will be charged interest on any payments made by JPM/BS from payment date to the closing date. This excludes funding related to unfunded commitments on commercial mortgage loans.
4. The LLC will receive interest credit or will be charged interest on any realized gains/losses from the date realized to the closing date.

- The day count convention used in calculating the cost of carry and reinvestment earnings credit was actual/360.
- The Primary Credit Rates in effect during the individual periods noted below from March 14, 2008 to close were obtained from the FRBNY's discount window as follows:

Primary Credit Rates

Effective date	New York Rate
04/30/08	2.25%
03/18/08	2.50%
03/17/08	3.25%
01/30/08	3.50%

Source: http://www.frbdiscountwindow.org/historicalrates.cfm?hdrID=20&dtlID=52

Ref: Primary credit rates from the FRBNY's discount window - Section Lead - Lead Schedules

Pre-closing date proceeds

Initial pre-closing date proceeds

- The table below presents the estimated initial pre-closing date proceeds associated with certain eligible assets and hedges for the period from March 14, 2008 to the cut-off date for each asset class as reconciled by EY, BLK and BS. These cash flows aggregated $606.2 million, which includes:
  - Cash flows from P&I, fees, and sales (to the extent there were sales of securities or loans during the period);
  - Reinvestment earnings credit related to cash flows from P&I, fees and sales; and
  - Cost of carry on the purchase price of $30 billion including the cost of carry of $40.7 million on the total value (carrying value plus accrued interest) of U.S. Treasuries transferred to the LLC aggregating to $5.9 billion.

Estimate initial pre-closing date proceeds

Currency: $000	Notes	Mortgage and U.S. Treasury securities	Commercial mortgage loans	Residential mortgage loans	Total
Cash flows from P&I, fees and sales		609.6	206.5	36.1	852.2
Reinvestment earnings credit related to cash flows from P&I, fees and sales	1	2.8	Post-close	0.2	2.9
Cost of carry on purchase price	2	(180.8)	(57.1)	(10.9)	(248.8)
Net cash flows		**431.6**	**149.4**	**25.3**	**606.2**

Source: Summary of Pre-Closing proceeds reconciliation_v4.xls

Ref: Estimated pre-closing date proceeds - Section Lead - Lead Schedules

1 The reinvestment earnings credit on commercial mortgage loans' P&I, fees and sales were excluded from the pre-closing date proceeds settlement at closing (see discussion below).

2 The cost of carry on purchase price of $180.8 million includes the cost of carry on $30 billion purchase price and U.S. Treasuries less the cost of carry on purchase price of commercial and residential mortgage loans presented separately.

Furthermore, the following items were noted during the course of our work:

Mortgage securities cash flows

- Cash flows from sales of 26 mortgage securities totalling $7.1 million included sales of 25 mortgage securities that were not approved by BLK, in its capacity as the asset manager and advisor to the FRBNY. The sales proceeds included in the cash flows related to these "unauthorized" sales were equal to the March 14, 2008 purchase price of these securities $5.1 million instead of the actual proceeds received by BS of $4 million. As agreed among the FRBNY, BLK and JPM, a true up may be made post close if BS is able to produce the appropriate documentation related to these sales.
- There were 15 eligible mortgage securities, which were fully paid off and one eligible mortgage security partially redeemed post-March 14, 2008. These securities, with an aggregate value of $23.2 million, were not delivered to the LLC given that they were already redeemed prior to closing. However, the LLC is entitled to all the cash flows from March 14, 2008 to the date when the securities were redeemed or paid in full. The total cash flows received on these mortgage securities for the period from March 14,

2008 to May 16, 2008 were approximately $13.1 million. The cash flows included in the pre-closing date proceeds remitted to the LLC at closing were $10.1 million less than the price paid for these securities given the cut-off date of May 16, 2008 for the cash flows related to eligible securities. Post-close, the analysis of cash flows related to redeemed securities will need to be updated in order to account for all the cash flows related to redeemed securities not actually delivered to the LLC and determine whether there are any significant shortfalls in cash flows related to these securities.

- The eligible mortgage securities included an X-1B security with a zero carrying value as of March 14, 2008. This security was issued as part of a CMBS transaction into which BS and BofA contributed floating rate commercial mortgage loans. As a result, we were told, BS and BofA share the cash flows from the security, which are based on the excess of the weighted average coupon on the remaining underlying loans over the weighted average coupon on the remaining bonds. We understand there is no written agreement between BS and BofA relating to the sharing of the cash flows since they disagreed on the manner of calculation. As a result, BS and BofA both agreed to calculate the cash flows separately and perform a true up every three to six months. At closing, the LLC received cash flows from the underlying security, which include amounts that would need to be paid to BofA post-close. Using the revenue sharing model provided by BS as a basis to estimate the amount owed to BofA, it was estimated that BofA's share of the cash flows from this security for the period from March 14, 2008 to May 16, 2008 was approximately $1.2 million.

Commercial mortgage loans cash flows

- The reinvestment earnings credit on P&I, fees and sales associated with eligible commercial mortgage loans of approximately $1.1 million was calculated and reconciled by EY, BLK and BS. However, given that this amount was excluded from the schedules to the trust and master servicing agreement, the amount was removed from the settlement of initial pre-closing date proceeds at closing. This amount will likely need to be included in the true up of cash flows post-close.

The following table below presents other cash flows related to commercial mortgage loans that were settled at closing:

Other cash flows settled at closing:	Total
Currency: $000	
Other cash flows settled at closing:	
Unfunded commitments	330,525.3
Rate lock reserves	8,229.3

Source: Summary of Pre-Closing proceeds reconciliation_v4.xls
Ref: Estimated pre-closing date proceeds - Section Lead - Lead Schedules

Pre-closing date proceeds

- At closing, the par value of remaining unfunded commitments of $330.5 million and the corresponding rate lock reserves of $8.2 million were funded by BS into a delayed draw account. The delayed draw account was established for the future funding of the remaining unfunded commitments assumed by the FRBNY. Rate lock reserves of $8.2 million represent deposits related to commercial mortgage loans with unfunded commitments as protection to the lender. We understand these reserves will be refunded to the borrowers when the remaining loan commitment has expired or is fully funded.
- In connection with eligible commercial mortgage loans, BS received 3rd party reserves, which aggregated $1.7 million at May 31, 2008, representing deposits made by the borrowers for the future payment of miscellaneous loan expenses including legal, documentation, and appraisal, among others. At closing, it was unclear as to whether these reserves should remain with BS. The FRBNY indicated to us that this issue will be resolved post-close.

Residential mortgage loans cash flows

- The reinvestment earnings credit on P&I and fees associated with residential mortgage loans were estimated based on an assumption that cash was received at month end for March and April cash flows included in the initial pre-closing date proceeds.
- In addition, the estimated initial pre-closing date proceeds related to residential mortgage loans were no longer adjusted for the 32 loans removed prior to closing. As a result, a true up of the cash flows, along with the reinvestment earnings credit calculation, related to residential mortgage loans will need to be made post-close.
- The P&I aggregated on loans serviced by EMC are presented gross of servicing fees, as servicing fees were not charged by EMC to BS. The cash flows aggregated on loans serviced by Wells Fargo are presented net of the servicing fees charged by Wells Fargo. The FRBNY, BLK and JPM agreed to deduct EMC servicing fees as part of the post-close true up.

Cost of carry on purchase price

- The cost of carry on the purchase price settled at closing was calculated based on $30 billion of purchase price. However, due to adjustments to the purchase price, the purchase price was reduced to $29.97 billion. A true up of the cost of carry on the aggregate purchase price may need to be made post-close including any adjustments to the purchase price as a result of post-close work.

Macro and non-credit hedges

Macro and non-credit hedges

Eligible macro and non-credit hedges

Currency: $000	Count	Carrying value at 3/14	Accrued interest	Total
Eligible non-credit hedges included in the purchase price:				
Options on futures	4	21,428.9	n/a	21,428.9
Equity options	12	(3,404.0)	n/a	(3,404.0)
Total		**18,025.0**		**18,025.0**
Eligible macro and non-credit hedges with zero purchase price:				
Eurodollar futures	14	-		
Treasury steepener futures	1	-		
Treasury futures	1	-		
Equity shorts	14	-		
TBAs	25	-		
Total		-		
Eligible macro hedges transferred via repo and reverse repo:				
U.S. Treasuries (Steepeners)	17	5,865,646	3,719	5,869,365

Source: Non_credit_hedges_mort_gots_send_060308.xls from BLK, 6/10/2008
Ref: Eligible macro and non-credit hedges - Section M - Macro and Non-Credit Hedges

Eligible macro and non-credit hedges

- The LLC acquired macro and non-credit hedges along with the securities and loan portfolio included in the collateral pool. The macro hedges include curve steepeners (U.S. Treasuries) and equity shorts while non-credit hedges include equity put option contracts, future contracts, option on future contracts, U.S. Treasuries and To-Be-Announced ("TBA") mortgage securities. Similar to CMBX and IRS positions, no demarcation guidelines were established for the identification of eligible macro and non-credit hedges. The determination of eligible macro and non-credit hedges was negotiated between BLK, in consultation with the FRBNY, and JPM. Furthermore, certain eligible hedges were allocated between the LLC and JPM/BS based on a pop analysis performed by BLK, in consultation with the FRBNY and JPM and negotiations taking into account whether related assets were being transferred to the LLC (see Appendix A for the demarcation guidelines provided by BLK). Therefore, EY received a schedule of eligible macro and non-credit hedges negotiated among the FBRNY, BLK and JPM as summarized in the tables to the left.
- As discussed in the *Transaction overview* section, certain non-credit hedges acquired by the LLC including Eurodollar and Treasury futures, TBAs, U.S. Treasuries, and equity shorts shown in the table to the left did not result in specific cash purchase price to be paid by the LLC at closing and as a result required no additional funding by the FRBNY.
- As also discussed in the *Transaction overview* section, U.S. Treasuries were transferred to the LLC via repurchase and reverse repurchase transactions.
- The portion of certain macro and non-credit hedges allocated to the LLC's portfolio was rounded to the nearest $1 million of notional amount for U.S. Treasuries, the nearest contract for futures and options and the nearest share for equities as negotiated between BLK, in consultation with the FRBNY, and JPM.

Comparison with supporting documents

Comparison of eligible assets and hedges with supporting documents

Eligible mortgage securities by custodian

Currency: $millions	Count	Original face value or Notional	Carrying and agreed value
Held at JPM	1,163	37,572.3	11,168.8
Held at DTC	134	2,149.1	699.9
DTC pledged to JPM	1,052	70,902.6	4,877.5
Euroclear	6	26.0	16.2
Total	**2,355**	**110,650.0**	**16,762.4**

Source: Comparison with custodians
Ref: Mortgage securities by custodian - Section S - Securities

Documentation deficiencies or exceptions

During our work, there were differences or exceptions identified in comparing the list of eligible assets and derivatives with supporting internal or external documentation. However, based on the FRBNY's negotiations with JPM, these differences or exceptions did not warrant removal or exclusion of these assets or hedges from the eligible portfolio.

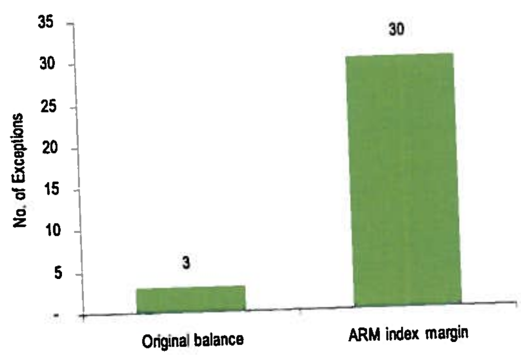
Mortgage securities

- The original face values of 2,355 eligible mortgage securities were compared to externally obtained custodian or clearing statements as of March 14, 2008 and subsequent periods through May 16, 2008 to reconcile the mortgage securities that are to be delivered by BS to the LLC upon closing of the transaction.
- The table to the left presents the original and carrying value (excluding accrued interest) of the eligible securities by custodian or clearing balance. Of the 2,355 eligible mortgage securities, 1,297 securities with a carrying value of $11.9 billion were compared to JPM custodian statements and the Depository Trust Company ("DTC") clearing statements provided by BS. For 1,052 eligible securities with a carrying value of $4.9 billion that were pledged to JPM by DTC to be used under a tri-party repurchase agreement, DTC was unable to provide back dated March 14, 2008 custodian reports due to what we were told were system limitations. As an alternative procedure, a listing of pledged BS inventory pledged to JPM by DTC was independently obtained from JPM. For the remaining 6 mortgage securities with a total carrying value of $16 million, a Euroclear clearing statement was independently obtained from Euroclear to reconcile the original face value presented in BS' internal reconciliation.
- During the course of our work, we identified 26 eligible mortgage securities that were sold and 15 mortgage securities that were redeemed in fully paid off or partially redeemed. Given that these securities were either sold or redeemed, the securities were not delivered to the LLC at closing. However, the cash proceeds from these securities were paid to the LLC at closing or will be paid to the LLC post-close (see related discussion in the *Pre-closing date proceeds* section).
- 2,269 securities were reconciled with the custodian or clearing statements at March 14, 2008 and 84 securities had differences related to fails to receive/deliver, cancel and correct transactions, DVP repo and reverse repo. However, except for the securities sold or redeemed as discussed in the *Pre-closing date proceeds* section, all the eligible mortgage securities that were expected to be delivered at closing appear to have been delivered to the LLC based on discussions with BLK, the FRBNY and State Street Bank, the FRBNY's administrator.

Comparison of eligible assets and hedges with supporting documents

Eligible commercial mortgage loans' unmatched attributes

Source: Commercial US Loan File Transfer as of 03.14.08 - E&Y v2Received5_22_08.xls, Commercial loan documents



Commercial mortgage loans

- For all eligible commercial mortgage loans, the attributes from the JABBA dataset, presented in the table below, were compared to signed / executed loan documents or external servicer documents, as applicable.

Commercial mortgage loans attributes

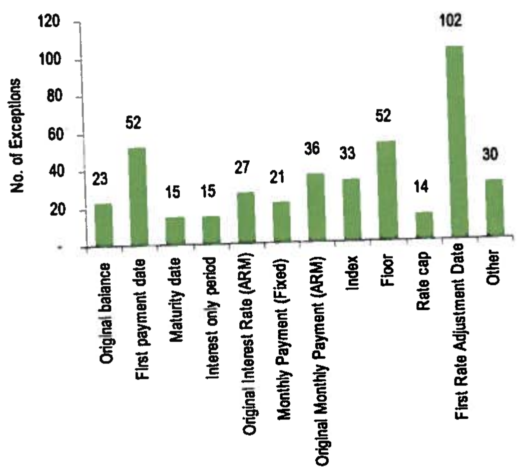
Attribute
Original balance
Current balance
Maturity date
Interest only period
Interest accrual type
Interest rate
Monthly debt service
Index
Floor
ARM index margin
LIBOR Strike

- A total of 33 attributes were unmatched, relating to 33 commercial mortgage loans with a current balance of $4.0 billion and carrying value of $3.7 billion as of March 14, 2008. The chart to the left summarize the exceptions identified in comparing the JABBA dataset to loan documents / external servicer documents.
  - Differences were noted in the original balances of 3 commercial mortgage loans between JABBA and loan documents/external servicer documents aggregating to $26.3 million. These differences; however, did not impact the current balance or carrying value of the eligible commercial mortgage loans.
  - Differences were noted in the ARM Index Margin related to 30 of the Hilton loans (all senior loans and mezzanine loans A through H) between JABBA and the loan agreements, which represents a difference of approximately 0.00033%. BS management has represented that a small paydown occurred in February 2008, which prompted the minor adjustment in margins. However, since the first and second amendments to the loan agreement and loan documents provided by BS, which are dated December 15, 2007 and May 30, 2008, respectively, it does not appear that this minor change in margin was documented. It should be noted that the ARM Index Margin as recorded in the March 14, 2008 JABBA dataset was reconciled with the March 2008 remittance report.

Comparison of eligible assets and hedges with supporting documents

Eligible residential mortgaged loans' unmatched attributes

Source: Available Inventory - Final Loan List v3B final all data xls, Loan documents, Servicer reports



Residential mortgage loans

A sample of residential mortgage loans was selected for comparison with loan documents and information from the servicers (see chart to the left and table below for a summary of the sample population selected). The following sampling methodology was provided by the FRBNY:

- Select at least 10% of the loans in the of the following categories:
  - Current balance groupings – $0.00 to $499,999.99 and $500,000.00 to $999,999.99
  - Servicers – EMC and Wells Fargo
  - Rate type – Adjustable and Fixed
- Select all loans with a current balance equal to or greater than $1,000,000.00

Summary of residential mortgage loan sample

	Fixed			ARM			TOTAL		
Currency: $millions	Loan count	Current balance ($)	% of Total Eligible Fixed	Loan count	Current balance ($)	% of Total Eligible ARM	Loan count	Current balance ($)	% of Total Eligible
EMC Mortgage Company									
0.00 to 499,999.99	672	51.8	7.37	320	73.0	6.90	992	124.7	7.09
500,000.00 to 999,999 99	22	14.1	2.00	42	27.1	2.57	64	41.2	2.34
1,000,000.00 or greater	11	14.3	2.03	42	50 9	4.81	53	65.2	3.70
	705	**80.1**	***11.40***	**404**	**151.0**	***14.28***	**1,109**	**231.1**	***13.13***
Wells Fargo									
0.00 to 499,999.99	94	10.1	1.43	70	12 2	1.15	164	22.2	1.26
500,000.00 to 999,999 99	6	3.7	0.53	9	6.7	0.63	15	10.4	0.59
1,000,000.00 or greater	3	5.1	0.72	7	12 3	1.17	10	17.4	0.99
	103	**18.9**	***2.68***	**86**	**31.2**	***2.95***	**189**	**50.1**	***2.84***
Total sample	**808**	**99.0**	***14.08***	**490**	**182.2**	***17.23***	**1,298**	**281.2**	***15.97***
Total population	**7,122**	**702.7**	***100.00***	**3,864**	**1,057.7**	***100.00***	**10,986**	**1,760.3**	***100.00***

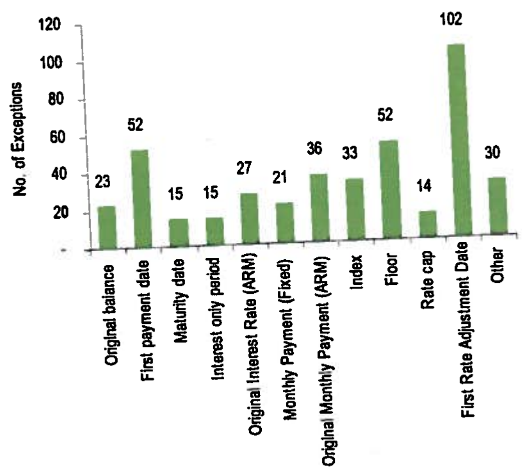
Source: Ava lable Inventory - Final Loan List v4 final.xls

Ref. Summary of residential mortgage loan sample - Section E - Comparison with supporting documents

Comparison of eligible assets and hedges with supporting documents

Eligible residential mortgaged loans' unmatched attributes

Source: Available Inventory - Final Loan List v3B final all data.xls, Loan documents, Servicer reports



- The attributes from the WITS dataset, presented in the table below, were compared to signed/executed loan documents or servicers reports (which includes SBO 2000, Fidelity and external servicer reports), as applicable, for the sample of eligible fixed and adjustable rate residential mortgage loans agreed to by the FRBNY.

Residential mortgage loans attributes

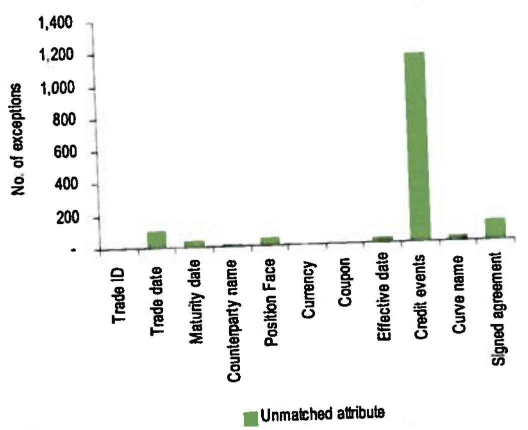
Attributes
All loans:
Original balance
Current balance
Next due date
Paid through date
Servicing fee
First payment date
Maturity date
Interest only period
Fixed-rate loans:
Fixed Interest Rate
Monthly Payment (Fixed)
Floating-rate loans:
Original Interest Rate (ARM)
Current Interest Rate (ARM)
Original Monthly Payment (ARM)
Current Monthly Payment (ARM)
Index
Margin
Floor
Rate cap
First Rate Adjustment Date
Payment Adjustment Frequency
Rate Adjustment Frequency

- A total of 420 attributes were unmatched, relating to 266 residential mortgage loans with a current balance of $81.2 million and carrying value of $72.0 million as of March 14, 2008. The chart to the left summarizes the exceptions identified in comparing the WITS dataset to loan documents / external servicer documents.

Comparison of eligible assets and hedges with supporting documents

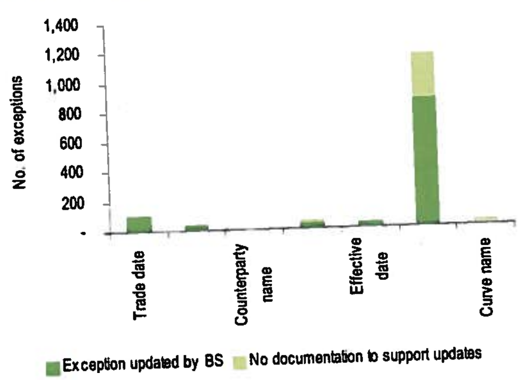
Eligible single CDS' unmatched attributes

Source: Yelisayev.Black_Rock_FED_WhiteBook2700_Derivatives_Trades_Mar14(6) - 5.28.08.xls (Swap/ Derivclear population), SwapDerivClear_061708_send_E&Y.xls (BLK); Hardcopy Confirmations



Exceptions related to eligible single name CDS

Source: Yelisayev.Black_Rock_FED_WhiteBook2700_Derivatives_Trades_Mar14(6) - 5.28.08.xls (Swap/ Derivclear population), SwapDerivClear_061708_send_E&Y.xls (BLK); Hardcopy Confirmations



Credit derivatives

- The eligible single name CDS positions as of March 14, 2008 identified from SWAP/Derivclear were compared to DTCC, executed external trade confirmations, or internal trade tickets. DTCC is an industry-wide service provider most commonly used to confirm credit derivatives, but is also used to confirm interest rate derivatives, and has recently been used to facilitate settlement of DTCC-eligible trades.
- 122 positions, with a total carrying value of $72.0 million, were internal transactions, for which confirmations do not exist. These internal transactions were compared to trade tickets provided by BS. Various attribute exceptions were noted for 1,231 of the positions compared to executed external ISDA trade confirmations, and 39 of the positions compared to trade tickets.
- The majority of the exceptions were noted in the following unmatched attributes: credit events, trade date, and position face.
- There were 1,409 exceptions noted from comparison of trade terms and attributes to ISDA confirmations or trade tickets. BS management has represented that these 1,409 differences have been updated in the respective system and has provided screen prints demonstrating the adjustments made in the respective systems for 1,071 positions. However, BS did not provide any documentation indicating the adjusted trade terms and attributes for 338 of the exceptions. BS management has represented that such adjustments or updates recorded did not have an impact on the carrying value of its derivative positions, but provided no evidence to support such assertion. The FRBNY may want to obtain such evidence post-close.

CMBX

- There were 1,927 CMBX positions from which the 26 eligible CMBX series were identified. These 1,927 CMBX positions were comprised of 1,596 external trades and 331 intercompany trades where both counterparties to the trade are internal BS entities. The 1,596 external trades were compared to DTCC or external ISDA positions.

Interest rate derivatives

- The trade terms and attributes for 153 of the eligible IRS positions were matched with internal trade tickets without exception. A total of 10 exceptions were noted on 6 of the eligible IRS positions. For these exceptions, the trade tickets did not agree to the details in the SWAP/ Derivclear file, as incorrect data was pulled into the SWAP/Derivclear file. Subsequently, BS provided screenshots from SWAP/Derivclear demonstrating that SWAP/Derivclear (as updated) matched the trade ticket without exception.

Comparison of eligible assets and hedges with supporting documents

Macro and non-credit hedges (presenting notional, number of contracts and number of shares).

	Count	Notional of eligible positions allocated to the LLC (after rounding)	No. of contracts (actual) of eligible positions allocated to the LLC (after rounding)	No. of shares (actual) of eligible positions allocated to the LLC (after rounding)
US. Treasuries	17	5,790,000.0	n/a	n/a
Equity shorts	14	n/a	n/a	(12,749,319.0)
Equity put options	12	n/a	(13,628.0)	n/a
Eurodollar futures	14	n/a	(5,078.0)	n/a
Treasury steepener futures	1	n/a	15,585.0	n/a
Treasury futures	1	n/a	26.0	n/a
Options on futures	4	n/a	9,300.0	n/a
TBAs	25	(6,514,000.0)	n/a	n/a

Source: Non_credit_hedges_mort_gots_send_060308.xls from BLK, 6/10/2008
Ref: Macro and non-credit hedges (by product type) - Section M - Macro and Non-Credit Hedges

U.S. Treasuries

- The notional amounts (prior to allocation to the LLC and rounding) of the eligible U.S. Treasury positions were reconciled with BS' Treasury stock records. Given that the U.S. Treasury stock records contain not only the mortgage desk's positions but includes the entire BS' holdings at March 14, 2008, the comparison was performed to the extent that the original face value of the eligible U.S. Treasury positions is less than the original face value presented in the Treasury stock record.

Equity shorts

- The number of shares of eligible positions (prior to allocation to the LLC) was compared to BS's back-office reports and historical stock record listing, which presents BS' inventory positions at March 14, 2008. There were no differences between the shares provided by BLK and BS' back-office reports. The prices of these equity shorts at March 14, 2008 were not provided by BLK. BS provided back-office reports, which showed the prices and carrying values of these equity shorts in BS' books at March 14, 2008.

Equity put options

- The contract size and carrying value of 12 eligible equity put options (prior to the allocation to the LLC) were compared to BS' back-office reports at March 14, 2008. We noted a difference of approximately $269 thousand in one equity put position (DJIS55660) based on the information contained in the MORT to GOTS and ADP reconciliation. BS management has represented that the carrying value was incorrectly calculated in the MORT to GOTS and ADP reconciliation. An adjustment was made to appropriately reflect the carrying value of this equity position included in the purchase price.

Futures and option on futures

- The actual contract amount (prior to allocation to the LLC and rounding) of the eligible futures and options on future contracts were compared to BS' daily trade blotter and register, which are provided to BS by the exchanges on a daily basis. The daily trade blotter and register include BS' entire inventory of futures and options on futures at March 14, 2008. As such, the comparison was performed to the extent that it can be determined that the contract amount of the eligible futures and options on future contracts is less than the amount presented in the daily trade blotter and register.

To-be-announced ("TBA") mortgage-backed securities

- Given that the carrying values of eligible TBAs were agreed between BLK and JPM to be based on Lehman Live, only the notional values of eligible TBAs were compared to BS' back-office reports. BS provided back-office reports that include the eligible TBAs on a position level basis, which were reconciled to the notional amounts of eligible TBAs to be transferred to the LLC.

Marks analysis

Marks analysis

As noted in the Transaction overview section, the values of eligible assets and hedges were generally based on the marks or prices in BS' books and records at March 14, 2008. The commentary presented in this section of the report is a high-level description of BS' mark-to-market or valuation process and is based solely on discussions we had with representatives of BS. No independent testing or verification was performed on these processes, except for certain mortgage securities that had prices at March 14, 2008 published by independent pricing vendors such as IDC, Reuters or Bloomberg.

Mortgage securities

Mortgage securities positions include positions in ABS, CDOs, CMOs, US Treasuries, agency mortgage securities, and listed futures and options. These mortgage securities are marked on a daily basis utilizing external market prices, if available, internal proprietary models, overall market knowledge, internal and external research reports, and overall market knowledge to calibrate model inputs for each security.

Daily valuation process

- Daily pricing is typically performed through a matrix approach using benchmarks to determine pricing relative to movement in the associated benchmarks. Certain mortgage securities may be modeled through FAST or other cash flow models when certain pricing parameters for the mortgage securities might have changed, although this is typically more a month-end process. While price indications from other dealers or source vendors may serve as inputs to the pricing process, FO traders typically view them as secondary sources. The internal BS models are maintained by the FAST group, the BS internal FO research group, responsible for maintaining proprietary pricing models as well as economic and econometric models used to derive a variety of bond model inputs, including, but not limited to, loan prepayment rates, default rates, and interest rate assumptions.

Monthly verification process

- Independent mark verification is performed on a monthly basis by both MBS BUC and RM. Product Control, in conjunction with the FO, tracks the daily P&L movement at the sub-group or desk level, which can include hedge positions. Policy requires that Product Control monitors the daily P&L and any related FO explanations to identify abnormal or unexpected movements. For liquid mortgage securities with available independent third party marks, MBS BUC reviews marks by comparing the FO marks to the marks available from independent pricing vendors, such as IDC and Reuters, on a monthly basis. For illiquid mortgage securities with few or no available marks, RM reviews the FO marks on a monthly basis, using FAST models and internal and external research reports.

Marks analysis

Mortgage securities pricing comparison

- BS FO carrying values as of March 14, 2008, for the population of eligible mortgage securities, were compared to values derived from prices independently obtained from Reuters, IDC, and Bloomberg, as well as the available Pricing Direct prices provided by BS. Pricing Direct is an internal pricing service that BS offers externally to clients and is a service provided independent from BS trading and BO functions. For those positions where marks were available from more than one external source, the lowest mark was utilized for the comparison against the BS FO carrying values. BS FO carrying values on the eligible securities were also compared to the values utilizing the Pricing Direct marks. Prices produced by Pricing Direct do not necessarily reflect BS books and records prices. Pricing Direct only produces prices for specific mortgage securities requested by BS clients. The initial Pricing Direct price file of mortgage securities requested by BS customers was used for this analysis.
- A total of 2,355 eligible mortgage securities were identified as of March 14, 2008, based on demarcation guidelines, with a total carrying value of approximately $16.8 billion based on BS FO marks. Of the total 2,355 eligible mortgage securities, 611 CUSIPs (approximately 25.9% of the total eligible CUSIPs) had no available mark from an external pricing source (i.e., IDC, Reuters, or Bloomberg) or Pricing Direct. The total value for these securities was approximately $6.3 billion, representing approximately 37.6% of the total carrying value of eligible mortgage securities.

The following table presents the results of comparing BS' carrying value for eligible mortgage securities with available external marks (from IDC, Reuters or Bloomberg) or Pricing Direct mark:

Results of comparison with external and pricing direct marks

Currency: $millions	Count	Carrying value	Pricing Direct mark	Lowest external mark	Average external mark	Highest external mark
Comparison with external mark:						
Value of eligible mortgage securities with external mark	1,687	9,191.1				
Value of eligible mortgage securities based on external marks	1,687			9,065.7	9,668.1	9,366.9
Difference compared to external marks				125.3	(175.8)	(477.0)
Comparison with Pricing Direct:						
Value of eligible mortgage securities with Pricing Direct mark	693	6,511 9				
Value of eligible mortgage securities based on Pricing Direct marks	693		6,550.1			
Difference compared to Pricing Direct marks			(38.2)			
Value of eligible mortgage securities with no external or Pricing Direct mark	611	6,294.6				

Source: EY analysis
Ref: Comparison with external and pricing direct marks - Section S - Securities

Ernst & Young

Marks analysis

- The total carrying value of 1,687 eligible mortgage securities with available external marks is $125.3 million greater than the total value obtained using the lowest external prices, $175.8 million less than the total value obtained using average external prices, and $477.0 million less than the total value obtained using highest external prices.
- The total carrying value of 693 eligible mortgage securities where Pricing Direct marks were available, was approximately $38.2 million less than the value obtained using Pricing Direct marks.

Commercial mortgage loans

The commercial securitization book consists of commercial mortgage loans to be sold into securitizations. It was indicated by BS management that some loans were originated with the intent of holding them on balance sheet. The commercial macro hedge book is used to execute hedges, primarily through derivative contracts, against the loans in the commercial securitization book. These books together are referred to as the commercial conduit or the commercial securitization conduit.

Daily valuation process

- Commercial mortgage loans are marked by the FO based on their evaluation of market movements, available market indicators, and internal BS models. Product Control, in conjunction with the FO, monitors the daily P&L movement at the sub-group or desk level, which may include hedge positions, and obtains any related explanations to identify abnormal or unexpected movements.
- The FO marks loans for technical factors, based on available market data, where available, and other market factors. However, not all loans are marked on a daily basis. Typically, BS identifies several loans as "markers" and adjust the price of these loans to reflect the total expected change impacting the portfolio of loans. A more robust pricing process that considers loan specific fundamentals occurs, at a minimum, on a monthly basis with an "ad hoc" pricing exercise occurring during the month if there are any significant events, changes in market conditions or situations that dictate further review of the loans. Since most commercial mortgage loans have penalties that limit prepayments, spreads for either securitizations or whole loans (as described below) and interest rates are usually the inputs that typically drive valuations in the pricing process, where markets are liquid and data is available. This also limits the need for complex models for pricing, although the FO has access to the FAST model library where models might be applicable (e.g., securitization models).

Monthly valuation process

- At month-end and on an "ad hoc" basis, loans are evaluated by the FO based on more deal specific fundamentals and the exit price for the type of loan and its characteristics. Loan values are adjusted based on BS management's view of their market value and during this process, the gain or loss on the "marker" loans is typically spread to the other loans. Loan level fundamental analysis will consider specific characteristics such as occupancy rates, rent levels, local market supply and demand and numerous other factors.

- RM performs reviews to validate the month-end marks for the commercial loan portfolio. RM reviews the fundamentals and assumptions behind the FO marks and the supporting rationale. RM challenges marks they believe are not reflective of the current market. Prior to the liquidity crisis, RM was not as involved in price validating commercial mortgage loans due to the fact that such loans were not owned and therefore were not on balance sheet for long periods of time and there were available marks through the exit pricing to securitization. As liquidity and securitization volume have decreased significantly, causing less available pricing, loans were held on balance sheet for longer periods of time. RM has increased its involvement in the month-end price verification process through its assessment of assumptions and model inputs.
- RM and FO use similar approaches in pricing commercial mortgage loans since they utilize the most current available market data, from whole loan sales or securitizations, to current market price. If there are no recent transactions for comparable loans, all current transactions are reviewed and a potential exit price is interpolated from currently available mark data. There is a high degree of subjectivity in the pricing process in the absence of an active market.

BS P&L remark of commercial loan portfolio

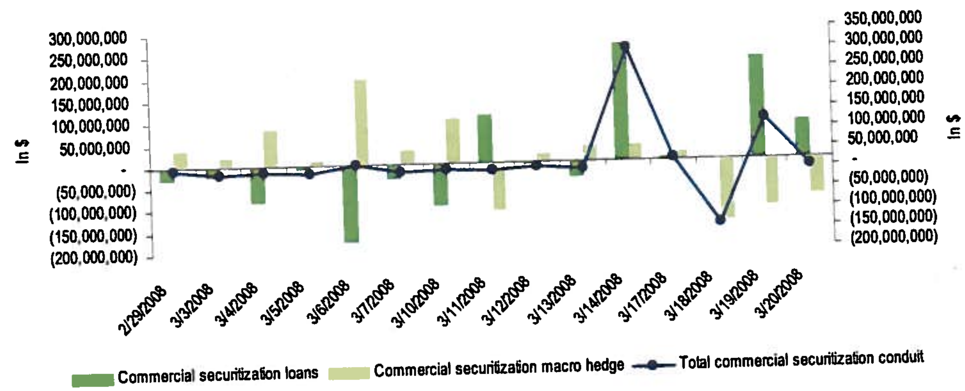
- As of March 14, 2008, BS remarked all of the commercial mortgage loans in the portfolio. The "marker" loans were marked up and other loans were reviewed for carrying value changes. It was noted that 17 commercial mortgage loans in the portfolio and an equity transaction (a position excluded from the portfolio), were marked up for a total increase in carrying value of $274.3 million. It was also noted that 107 commercial mortgage loans were marked down for a decrease in carrying value of $23.4 million. The net effect of these movements was a $250.9 million increase in carrying value (which includes approximately $100 million in equity transaction, which is excluded from the portfolio).

Daily P&L analysis

The chart below presents the commercial securitization conduit loans and correlated hedges daily P&L from February 29, 2008 to March 20, 2008.

Commercial securitization conduit: loans and hedge daily P&L

Source: MBS MRS P&L reports provided by BS BUC



- The commercial securitization conduit sub-group maintains a single hedged book comprised of the commercial securitization and commercial macro hedge books. It was noted that, during the period from February 29, 2008 to March 20, 2008, a close P&L offset existed between the loan and the hedge books for a majority of the days during this period. Instances of timing differences were also noted, where the value of the hedges would shift and the loans were remarked a day or two later. The chart above indicates that the daily net P&L for the commercial securitization and commercial macro hedge books, for the period from March 1, 2008 to March 20, 2008, was relatively flat with the exception of the spike on March 14, 2008, which represented the loan gains from a remark of various floating rate loans. It was noted that $141.6 million of the increase in the value of the loans was attributable to the price movements on seven loans with an aggregate adjusted carrying value of $937.3 million.

Marks analysis

Residential mortgage loans

BS separates their residential mortgage assets into the mortgage trading desk and the "scratch and dent" ("S&D") desk. The mortgage trading desk consists of residential mortgage loans that are current and are either originated by BS or purchased from a 3rd party. These loans are newly originated and are typically aged no longer than 6 months. The S&D desk consists of residential mortgage loans that have a history of missed payments or document deficiencies. These loans are aged approximately 2 or 3 years from their origination. For all loans BS owns and services, the applicable servicing fee income is included in the marks.

Mortgage trading desk

- The mortgage trading desk's process for marking residential mortgage loans is broken out by conforming and non-conforming loans.
  - Conforming loans (i.e., mortgage loans that conform to GSE guidelines) are placed into pools based on typical TBA pool characteristics such as coupon, term, and interest only or non interest only. The TBA pooled loans are marked to exit value in the TBA market.
  - Non-conforming loans are placed into product pools and marked at the pool level based on the similarities of particular loan profiles and their associated expected cash flow. No individual marks are given to loans in the pools as all loans mirror the mark of the pool.
- For the mortgage trading desk, loan pools are generally remarked (based on loan pool specific fundamentals) on a weekly basis by the desk. The loan pools are also marked daily against an associated hedge as these hedges are liquid and actively traded in the market.

S&D desk

- The S&D desk process for marking residential mortgage loans is different for performing vs. non-performing residential mortgage loans.
  - Non-performing residential mortgage loans are valued on an individual basis due to the nature of the asset. Non-performing assets are categorized in different stages, such as REO, foreclosure, bankruptcy, or work-out, and expected cash flows are projected on a case by case scenario.
  - Performing residential mortgage loans are marked at a pool level based on the similarities of particular loan profiles and their associated expected cash flow. Performing residential mortgage loans are defined by BS as being current on payments made between 0 and 59 days. The loans are marked to an exit value similar to the marking of the non-conforming mortgage loans described above using the securitization and whole loan pricing platforms.

- For the S&D desk, all the loan pools are remarked at month-end. An intra-month remarking will take place on the S&D desk if a significant event has occurred, which would warrant a remarking before month end. The loan pools are also marked daily against an associated hedge as these hedges are liquid and actively traded in the market.
- There were 4,139 loans (40% of eligible residential mortgage loans) included in the eligible portfolio that were identified from the "S&D" pools and were priced at loan level marks. These loans had an aggregate value of $576 million at March 14, 2008.

RM and Product Control review

- RM reviews the marks at month-end and challenges the assumptions used and the reasonableness of the marks compared to the market. On a daily basis, a flash report is produced and reviewed by Product Control. Product Control reviews for any significant movements and challenges any irregular activity. The models used by the traders to derive the marks on the pools are tested and reviewed by RM on an annual basis. These models are created and maintained by BS FAST group.

Mortgage Servicing Rights

- The population of eligible residential mortgage loans includes 9,501 loans serviced by EMC, with a current balance of $1.5 billion. EMC will retain the mortgage servicing rights ("MSR") associated with these assets. Under *SFAS 140, Transfers of Financial Assets*, a servicing asset or liability is created upon the sale or securitization of assets where the MSRs are retained by the seller. As agreed upon by the FRBNY, BLK and JPM, BS made an estimate of the value of the MSRs related to the eligible residential mortgage loans by applying the same MSR prices that BS used to value the MSR assets associated with other residential loans with the same product types. The MSR prices of these other loans were based on the MSR asset disclosed in BS' quarterly financial report to the SEC (Form 10Q) as of February 29, 2008.
- The estimated value of the MSRs as of March 14, 2008 retained by EMC totalled $14.6 million. The MSR value was deducted from the March 14, 2008 carrying value to calculate the final purchase price of the eligible residential mortgage loans.

Derivatives

Credit derivatives

- Derivative positions are marked periodically by the FO based on their evaluation of market movement, available market indicators, and results of internal BS models. There is no formal daily mark process established by BS. BS Product Control utilizes both externally available data and BS internal research inputs to the internal BS models. BS Product Control, along with the FO, tracks the P&L movement at the sub-group or desk level, which often includes both cash and derivative positions, and obtains any related FO explanations to identify abnormal or unexpected movements. Product Control generates and provides management reports outlining these movements.

- The eligible credit derivatives portfolio mainly consists of PAUG ABS CDS transactions. These are credit default swaps on single name ABS, which are priced by the FO based on the credit worthiness and performance (i.e., prepayments, defaults, credit events) of the underlying ABS securities. The derivatives portfolio also includes indices (i.e., ABX, CMBX) and tranche indices (e.g., TABX – Tranche ABX), which have prices sourced from Mark-it Partners, the third party company that determines, maintains and reports prices for these indices. In connection with this transaction, ABX and TABX trades were excluded from the eligible derivatives pool. Additionally, the portfolio includes CDSs on CDOs and CLOs and interest rate swaps to hedge interest rate exposure.

PAUG ABS CDS

- The FO follows two different approaches in marking the portfolio of PAUG ABS CDS derivative positions.
  - Bucketed "blip" method: The total portfolio of PAUG ABS CDS is categorized into buckets based on the original rating and vintage of the underlying ABS. An average ABS-bucket price is computed based on the prices of individual ABS securities contained in that particular bucket. Each bucket is mapped to a comparable ABX index. Changes in the price of the index are used to understand the changes in the price of the ABS in each BS bucket. This valuation methodology focuses on general characteristics such as ratings and vintages of the securities underlying the transactions and does not consider detailed aspects of the trades, such as credit event definitions or other factors such as loss coverage ratios.
  - Line by line valuation: This involves an assessment of the underlying ABS for each of the CDS trades. Traders use available market prices for comparable assets, market insight from other participants, internal and external research reports and internal FAST group models to arrive at a price for the underlying ABS. The carrying value of the CDS is calculated as the difference between a par value of 100 and the FO-determined price of the ABS, multiplied by the CDS Notional. Valuation under this approach would consider transaction specific attributes such as credit event definitions.
- PAUG ABS CDS are not required to be marked daily; however, they are marked using the blip method, at a minimum, on a monthly basis. A line by line valuation is rarely performed due to the time commitment required to process a large population of trades. However, when a significant market movement or deal specific event occurs, BS will typically employ the line by line approach on the potentially affected trades to determine carrying values.
- RM performs reviews on a monthly basis to analyze the month-end FO marks for the derivatives portfolio. Prior to November 30, 2007, RM was independently verifying FO marks for PAUG ABS CDS

using a third party consensus pricing source to obtain certain market inputs to its models (notably credit spreads and durations). The goal of the review process was to identify significant differences between FO and RM values, which could require valuation adjustments at month-end. After November 30, 2007, in response to the less active and decreased availability of market data in the credit markets, RM reduced its reliance on using consensus credit spreads and duration as key variables. RM began analyzing FO marks of the underlying ABS securities by calibrating the FAST group models using market movements from available indices and/or transactions.

CDS on CDOs and CLOs

- For CDS on CDOs, the FO utilizes several internal models for valuation purposes based on the characteristics of the specific transactions. In addition to market factors, other variables that can affect the valuation include whether the capital structure has a fixed or variable cap (which defines the amount available for payment to the buyer of protection) and whether it incorporates implied or non-implied write-downs (which defines the timing of the payments). These factors generally affect the pricing of the structures as they can alter the level and timing of payments received by the protection purchaser. Pricing can also require valuation of the underlying CDO using cash flow models and certain assumptions regarding the underlying CDOs, including expected time to default. Due to their specific nature, these transactions are only priced (and price validated by RM) on a monthly basis. These transactions also tend to have numerous deal specific reserves (fair value adjustments) depending on the nature and performance of the underlying CDOs.
- For CDS on CLOs, BS marks the positions with a basic spread approach. The difference in the spread associated with each CDS on CLO contract is compared to market spreads for comparably rated structures. The spreads associated with the underlying assets include market factors such as prepayments, default probability and other related considerations. The CDS value is the spread difference multiplied by the duration and multiplied by the contract notional value.
- For CDS on CDO's and CLO's, RM primarily relies on prices sourced by Mark-it Partners, an independent 3rd party source for prices and spreads on structured securities, where available to verify prices used by the FO. RM also uses liquidation values obtained from recently closed deals to perform qualitative assessments of FO prices.

Interest rate swaps

Interest rate swaps are valued using internal valuation models with market level inputs appropriate for the product being valued (LIBOR and/or Treasury curves, Swap rates, basis spreads and other parameters). Cash flows are projected into the future and are discounted along an appropriate curve.

Marks analysis

Credit valuation adjustment (CVA)

The CVA is computed by BS at the counterparty level based on the product of three components: 1) Probability of default ("PD") for each respective counterparty, 2) Loss given default ("LGD") for each respective counterparty, and 3) Exposure at default ("EAD") for each respective counterparty. For each time bucket in the future (e.g., 6 months, 1 year, 2 years, ..., 30 years), a CVA is calculated by multiplying EAD for each time bucket by the PD and LGD. The sum of the computed CVA at each time bucket is the total CVA at the counterparty level. BS then allocates the total CVA by counterparty to each trade using a weighted average methodology based on the significance of the expected market value (i.e., expected exposure) of each trade at a given period.

MRS adjustments

MRS adjustments

The commentary presented in this section of the report is a high-level description of BS reserving or valuation adjustments process and is based solely on discussions we had with representatives of BS.

- MRS adjustments are adjustments to earnings (P&L) and/or inventory (carrying values) that are "held back" by Product Control due to a number of different factors. MRS is a system that pulls information from other systems (mainly GOTS and Swaps/Derivclear) and acts as a centralized Product Control reporting tool for information related to values and profit and loss (P&L). BS management has represented that the MRS adjustments are recorded to more accurately reflect its P&L, but provided no further information and it is unclear why this information represents "better" information that serves as the basis to override marks otherwise made by BS systems.
- A large number of MRS adjustments represent timing differences that will be reversed when the differences are resolved. For example, amortization of paydowns on an ABS that will reverse against the receipt of the actual P&l, or valuation adjustments that are established as top-side entries and are reversed as the desk remarks individual transactions. MRS adjustments are typically evaluated at a sub-portfolio level and may apply across several products based on the trading strategy and marking policies of that portfolio. For example, ABX adjustment reserves reflect the profit or loss on the hedge of a portfolio (the ABX index) that are "held back" because the item it is hedging may not have been marked for that day. The adjustment would change each day as the hedge is remarked and would be released when the hedged item is eventually marked (at month-end, if not earlier).
- Adjustments are typically established by Product Control after discussion and review with FO and RM. Adjustments are recorded by Product Control in MRS and are applied to specific transactions or groups of transactions, typically within a specific portfolio within the Mortgage Desk. Product Control is responsible for monitoring and evaluating adjustments on an ongoing basis.

Types of MRS adjustments

- Product Control defines its MRS adjustments into various categories.
  - Market price changes: These are "real time" price changes to marks in the FO systems to reflect corrections or adjustments that did not make the overnight batch processing of the price feeds. These adjustments are generally made within one business day of the original pricing and are agreed to between the FO and Product Control. BS management has represented that the market price changes were reflected in the carrying values in the datasets provided (i.e., MORT to GOTS and SWAP/Derivclear files).
  - P&L reserves: Adjustments to reported P&L where the effects of changes in carrying value are "held back."

MRS adjustments

- Top-Side reserves: Portfolio or transaction level reserves that are recorded as top-side entries across a specific book. These reserves adjust for factors that effect positions at a portfolio level such as credit (i.e., CVA) or liquidity.
- Valuation reserves: Reserves for valuation changes of items in the portfolio that are entered as aggregate reserves due to the operational difficulties associated with changing of prices of individual line items.
- Cash reserves: Cash reserves reflect items where cash was received but has not been allocated or where cash was expected and has not yet been received. Each cash item is unique and their resolution requires an item by item review to identify proper allocation.
- Spread vs. Price Reserves (also Duration Reserves): Specific valuation adjustment required due to BS system pricing limitations for index based transactions (primarily ABX and CMBX).

Effect of MRS adjustments

- The effect of adjustments fall into three types: those that impact carrying value, those that affect P&L and those where the effect is dependent on the resolution of the difference that created the need for the adjustment.
- BS product control provided the February and March month end reserve reports and a detailed MRS reserves report as of March 14, 2008. The file contained a total of 1,077 items with a net adjustment value of negative $346.9 million. BS management has represented that these items cover all mortgage desk trading activities and therefore include items that may not be included in the eligible portfolios of securities, derivatives, and mortgage loans. It was noted that there were 188 negative adjustments greater than negative $1.0 million with an aggregate value of negative $1.8 billion, which were further analyzed through discussions with BS management and by obtaining supporting documentation related to the adjustments.

Remark of credit derivatives

- Based on the work we performed on the MRS adjustments, it was disclosed that certain credit derivatives were remarked and certain MRS adjustments, which impact carrying values, were not considered in the credit derivatives dataset provided for the demarcation process. BS management provided the analysis in the table below showing the net impact of carrying value adjustments aggregating approximately $107.2 million, of which $85.5 million had an impact on the eligible credit derivatives portfolio.

MRS adjustments

Allocation of CDS remark

Currency: $000	Net impact of adjustments to carrying value	Eligible IG Trades Selected	Eligible Non-IG Trades Selected	Trades to be Retained by JPM/BS	Unallocated	Total
Single Name RMBS	2,055	-	-	-	2,055	2,055
Delta Neutral	(388)	-	-	-	(388)	(388)
ARMs	75,861	53,379	24,401	(1,918)	(0)	75,861
RMBS Hedges in Correlation Book	11,893	(2,027)	2,678	11,241	-	11,893
CDO single names	(9,353)	4,622	(3,173)	(10,801)	0	(9,353)
CDO MRS Adjustments with no carrying value change	16,090	5,116	-	3,596	7,379	16,090
Commercial Secondary	11,486	17,916	(6,500)	39	31	11,486
All others	(420)	(420)			-	(420)
Total	**107,224**	**78,586**	**17,406**	**2,156**	**9,077**	**107,224**
% included for IG and Non-IG		100%	40%			
Impact on purchase price		**78,586**	**6,962**			**85,548**

Source: Allocation of CDS diff.xls (Pat O'Brien, 6/11/2008)

Ref: Allocation of CDS remark - Section Lead - Lead Schedules

Next steps

Next steps

Post-closing considerations

The following are items that the FRBNY should consider post-closing:

Mortgage securities

- Subsequent pre-closing date proceeds from May 17, 2008 to June 26, 2008 (including reinvestment earnings credit from May 17, 2008 to the date when actual payment is made to the LLC post-close).
- Update of the analysis of cash flows from May 17, 2008 to June 26, 2008 related to redeemed securities that were not delivered to the LLC at closing.
- Resolution on items that may need to be trued up post-close:
  - Potential purchase price adjustment related to CUSIP 90331HLG6.
  - Expected vs. actual accrued interest through March 14, 2008.
  - "Unauthorized" sales of mortgage securities.

Commercial mortgage loans

- Subsequent pre-closing date proceeds from June 1, 2008 to June 26, 2008 (including reinvestment earnings credit from June 1, 2008 to the date when actual payment is made to the LLC post-close).
- Resolution on items that may need to be trued up post-close:
  - Reinvestment earnings credit on the cash flows for the period from March 14, 2008 to May 31, 2008 that was excluded from the trust and servicing agreement and consequently excluded in the settlement of the initial pre-closing date proceeds at closing.
  - Whether the 3rd party reserves should remain at BS (i.e., side letter between the FRBNY and JPM on 3rd party reserves).
  - Update of rate lock reserve amounts held by BS.

Residential mortgage loans

- Subsequent pre-closing date proceeds from May 1, 2008 to June 26, 2008 (including reinvestment earnings credit from May 1, 2008 to the date when actual payment is made to the LLC post-close).
- Resolution on items that may need to be trued up post-close:
  - Update of estimated initial pre-closing date proceeds (including reinvestment earnings credit) from March 14, 2008 to April 30, 2008.
  - Adjustment to initial pre-closing date proceeds related to 32 loans removed prior to closing.

Next steps

- Servicing fees from March 14, 2008 to June 26, 2008.

Credit and interest rate derivatives

- Pre-closing date proceeds (including reinvestment earnings credit) from March 14, 2008 to June 26, 2008.
- Determination of cash flows resulting from transactions (e.g., terminations, novations, physical delivery, etc.) between March 14, 2008 and June 26, 2008.
- Quantification of potential adjustments resulting from position or notional differences that were identified prior to close.
- The FRBNY may want to obtain evidence supporting BS management's assertion that 338 of the exceptions noted in the comparison of single name CDS' trade terms and attributes to ISDA confirmations or trade tickets have been adjusted or updated in their respective systems.

Non-credit and macro hedges

- Pre-closing date proceeds (including reinvestment earnings credit) from March 14, 2008 to June 26, 2008 (i.e., determination of realized P&L between March 14, 2008 and June 26, 2008).
- Resolution on the differences in prices between BLK and BS related to equity put option and equity short positions that were covered subsequent to March 14, 2008.

Others

- The cost of carry on the purchase price settled at closing was calculated based on $30 billion of purchase price. However, due to adjustments to the purchase price, the purchase price was reduced to $29.97 billion. A true up of the cost of carry on the aggregate purchase price may need to be made post-close including any adjustments to the purchase price as a result of post-close work.

Due diligence procedures performed

Due diligence procedures performed

If used herein, the term "Review" does not constitute a review within the scope of the AICPA standards for Accounting & Review Services.

General

1 Read the Term Sheet including Schedules A and B and any subsequent updates to the schedules, and the final demarcation guidelines as provided. Gained an understanding of the details of arrangements and criteria for assets and hedges to be transferred to the LLC.

Quality of financial information

2 Obtained the full mortgage data set (including loan level data) specified in Schedules A and B of the Term Sheet downloaded from BS' back-office and middle-office systems and reconciled the data to the general ledger or its equivalent (e.g., SWAP/derivclear).

3 Obtained a reconciliation or explanation for differences identified.

4 Obtained credit ratings from Bloomberg or rating agencies for all mortgage securities included in the population to identify that all are investment grade and rated at least BBB- by one of Standard & Poor's, Moody's, and Fitch as of March 14, 2008, and determined that these are not rated lower by any of them.

Eligibility of assets and hedges

5 Documented the assets and credit hedges that are eligible using the filters specified in the demarcation guidelines.

6 Reconciled eligible assets and hedges identified using the demarcation guidelines with BLK's listing of eligible assets and hedges.

7 For residential and commercial mortgage loans, determined which loans are eligible by applying the filter specified in the demarcation procedures for loans (no more than 30 days past due). A loan was considered eligible if the "next payment due date" (as specified in the full data set of residential and commercial mortgage loans) is a date which falls on or after February 14, 2008. The resulting eligible residential and commercial mortgage loans were compared to BLK's list of eligible residential and commercial mortgage loans.

8 Reconciled the aggregate accrued interest related to eligible mortgage securities, loans and hedges (as applicable) identified as of March 14, 2008 and compared to BLK's and/or BS' calculations.

9 Investigated and obtained explanations for differences greater than $1,000 (actual dollars).

Eligibility of macro and non-credit hedges

10 Obtained the list of eligible macro and non-credit hedges negotiated between BLK, in consultation with the FRBNY, and JPM.

11 Obtained reconciliation of eligible macro hedges with books and records and reconciled identified eligible macro hedge with print-out or download of reports generated from BS middle- or back-office systems.

12 Obtained explanation for differences identified.

13 Computed the pro-rated portion of macro hedges using the pro-rata ratio defined in the demarcation guidelines, the Term Sheet or, in certain cases, provided by BLK, in consultation with the FRBNY.

Comparison of eligible assets and hedges with supporting documents:

14 For mortgage securities and commercial mortgage loans:

- Compared all eligible assets to supporting documents such as custodian statements, servicer reports, loan documents and/or DTC report on physical mortgage securities as of March 14, 2008.

15 For residential mortgage loans:

- Obtained reconciliation between BS and custodians as of March 14, 2008.
- For a sample of loans, compared eligible loans to supporting loan documentation focused on attributes that affect the economics of the loan cash flows (i.e., original balance, current balance, next due date, paid through date, servicing fee, first payment date, maturity date, interest only period, interest rates, monthly payments, index, margin, floor, rate cap, first rate adjustment date, payment adjustment frequency and rate adjustment frequency).
- Discussed residential loan sampling methodology with the FRBNY. EY presented the sample of loans identified to the FRBNY, which stratified the

Due diligence procedures performed

residential mortgage loans by servicer, loan size and loan type. The stratification criteria were amended based on guidance from the FRBNY.

16 For correlated and macro hedges:

- For exchange traded derivatives, compared eligible hedges to the respective exchange blotter/register or stock record allocation.
- For over-the-counter derivatives, determined if contract electronically matched on industry-wide confirmation or affirmation platform. If contract was not auto-matched, compared certain attributes (e.g., notional amount, reference obligation, credit event, among others) to signed counterparty confirmations.

Changes to eligible assets and hedges

17 Discussed any trades identified as potential circled trades at March 14, 2008 with BLK and the FRBNY to determine if these were to be included or excluded in the determination of eligible assets and hedges. Obtained supporting documentation related to potential circled trades from BS as deemed necessary. In connection with this transaction, circled trades relate to transactions negotiated or in process around March 14, 2008 that were finalized or documented after that date.

18 Obtained supporting documents for any trades conducted post-March 14, 2008 (e.g., sales related to eligible assets post-March 14, 2008).

19 Obtained data and supporting documents related to cash flows of eligible assets and hedges as well as trades executed and approved post-March 14, 2008 through pre-closing date for each asset class and aggregated associated cash flows.

20 Reconciled estimated pre-closing date cash flows with BLK and BS.

21 Obtained data supporting unfunded forward commitments as of March 14, 2008 related to eligible commercial mortgage loans.

22 Reviewed supporting documentation as well as carrying values for funded and unfunded portion and identified associated cash flows.

23 Obtained the list of approved trades post-March 14, 2008 from BLK (in its capacity as the asset manager and advisor to the FRBNY) and compared transactions related to eligible assets and hedges to determine whether or not they were approved by BLK.

24 Identified and resolved differences between BS and BLK provided information greater than $1,000 (actual dollars).

Review consistency of marks used on eligible assets and hedges

25 Discussed with BS and documented their pricing or valuation process flow from front office to back-office, any top-side adjustments (credit and liquidity reserves or mark-to-market adjustments), and process for trader overrides.

26 Reviewed how these overrides, adjustments, and reserves are allocated to the portfolio or various mortgage desks. Documented if such adjustments or overrides had an impact on the recorded value of eligible assets and hedges as of March 14, 2008.

27 Where available, compared marks on security positions in front office book with those provided to clients via BS' pricing service (Pricing Direct) or other pricing vendors used by BS as of March 14, 2008.

28 For additional mortgage securities positions identified after March 14, 2008, obtained negotiated marks between BLK, in consultation with the FRBNY, and JPM.

Appendix A

Demarcation guidelines

BLACKROCK SOLUTIONS®

Demarcation Rules for Maiden Lane Portfolio

Appendix to Ernst & Young 'Project LLC: Summary of Findings and Observations Report'
Provided by BlackRock Solutions November 2008

This document codifies the method by which assets in the Bear Stearns (BS) Mortgage Desk were identified as eligible for assignment to the Maiden Lane LLC as part of the transaction between the Federal Reserve Bank of New York (FRBNY) and JP Morgan (JPM). These demarcation rules were agreed between the FRBNY, JPM and BlackRock (BLK) prior to the close of the Maiden Lane portfolio on June 26, 2008.

These demarcation rules were further subject to a 'trimming' methodology, as described in the Ernst & Young *Project LLC: Summary of Findings and Observations Report*, in order to determine which of the 'demarcated' BS assets would be assigned to the LLC on June 26, 2008 under the transaction agreements.[1] The methodology was agreed between the FRBNY, JPM and BlackRock prior to the close of the Maiden Lane portfolio on June 26, 2008.

Section 1. Scope of the demarcation

Included in the scope of the demarcation are only i) the US dollar-denominated, US-domiciled assets in the Bear Stearns Mortgage Trading books, and ii) the US dollar-denominated, US domiciled hedges associated with these books. Demarcation rules apply based on the characteristics of the in-scope assets and hedges as of March 14, 2008. Trades which occurred on March 14 or prior but which settled after March 14 are considered executed trades and are therefore in scope[2].

[1] This document does not address documentation of the calculation of prices, market value, etc. or of pre- or post-close true up amounts
[2] Exceptions are residential whole loans, where unsettled trades are excluded

Section 2. Principles for demarcation of assets

The following filters are applied to the set of in-scope assets.

Section 2.1. Securities:

Eligible universe:

- The securities must be Investment Grade:
  - All securities rated lower than BBB-/Baa3 by any of S&P, Fitch or Moody's are excluded
  - Unrated securities are excluded[3]
  - All residuals (e.g., from CDOs, ABS, CMOs) are excluded, as these are unrated securities
- The securities must be assets:
  - Asset short positions are not considered assets
  - US Agency residential mortgage pools are excluded
  - Synthetics are excluded
- Other excluded categories are Mandatory Puts, Servicing, MBS Call Options, Prepay Penalties

Specific exclusions after reviewing the portfolio:

- Excluded US Agency IO/PO combos, as these were recombined into US Agency pools
- Excluded BSSP bonds
- Excluded 2 IO bonds with zero market value after discussion with BSC showed that these would not pay any additional interest
- Excluded 6 CDO-squared (i.e., CDOs composed primarily of other CDOs)

Eligible Non-Agency IOs were trimmed according to the trimming methodology documented by Ernst & Young.

[3] Excluded 7 CMBS/CRE CDO bonds which were identified in late May as having private ratings

Section 2.2 Residential Loans

Eligible universe:

- USD residential whole loans
  - Home Equity Line of Credit are excluded
  - Loans must be first or second ("junior") lien
  - Must be 100% participation by Bear[4],[5]
  - SBA (SBCA) loans are excluded
- Loans in the portfolio as of March 14
  - Pending Agency sales and Wells Fargo sales are excluded
  - Maturity date must be greater than 3/14/08
  - Unsettled sale trades as of 3/14/08 are excluded[6]
  - Loans with zero balance are excluded
  - Loans where current rate is zero are excluded
- Loans that were performing as of March 14
  - The loan is performing if it is not 30 days delinquent (or longer) as of March 14. (For clarification, rules used were: paid through date ≥ 1/14/08; this is equivalent to next payment date ≥2/14/08.
  - Loans where the servicer paid-through data or next due dates were not available/verifiable are excluded
  - MVBO book was excluded: These loans are EMC-serviced buyout loans on behalf of the MV Partners hedge fund and are not saleable.

Specific exclusions after reviewing the portfolio:

- Rounding differences - Used to reconcile ADP whole dollar positions to other systems. These positions do not represent actual whole loans.
- UPB Less than $500 - Low value loans with imminent maturity dates
- 130 DSI construction loans are excluded
- Small servicers are excluded (only loans where Wells, EMC and GMAC[7] are the primary servicer are included)

---

[4] HUD5/HD10/LIFE portfolios are excluded. Loans in these portfolios are 'participation' loans, where EMC shares in cash flow with a 3rd party

[5] Pended Loans (including NEMP) positions do not represent whole loan balances, but rather trailing payments (a 'receivable' for 1 or 2 payments due to EMC) on sold loans. Remainder of balance belongs to a trust.

[6] These were identified in the unsettled trade the report sent by Ed Lam of Bear Stearns on 5/14/08. The list of loans to be removed based on Ersnt & Young's due diligence was provided by Lakshman Kannan of Ernst & Young on 5/15/08 at approx. 2.32pm.

- 60 loans from 2 specific deals are excluded, as the BSC system showed that these deals were not in the books and records as of 3/14/08
- 4 loans that had a servicing transfer before 3/14/08 are excluded
- 62 loans with repurchase, litigation or side note issues are excluded
- 47 loans with custodian related exceptions are excluded
- 11 loans with documentation breaks are excluded[8]

Additional residential whole loans were excluded according to the trimming methodology documented by Ernst & Young.

Section 2.3 Commercial Loans

Eligible universe:

- Commercial loans in the BS Mortgage Trading books as of 3/14:
  - Current balance must be greater than 0
  - Maturity must be greater than March 14, 2008
  - Collateral held as part of the reverse repo agreement is not eligible
  - Equity positions in commercial loans excluded
  - Tax-advantaged commercial loans held outside the commercial mortgage desk are excluded
  - Revolving lines of credit are included
- Must be performing as of 3/14:
  - The loan is performing if it is not 30 days delinquent (or longer) as of March 14
  - Loan must be performing as of 3/14 according to the servicers
- Unfunded portions of committed commercial loan facilities are included
- Consent to transfer
  - Consent must have been obtained by May 20, 2008
  - This excluded Harrah's loan positions

Specific exclusions based on review of the portfolio:

- Excluded one loan DPO which settled on 3/19 (Green Street), as the trade was in progress prior to 3/14

[7] Note that subsequent trimming methodology excluded GMAC serviced loans
[8] Loans excluded due to missing documents

Section 3. Credit Hedges (excluding CDS and CMBX)

The investment grade, US dollar denominated, US domiciled credit hedges associated with the BS mortgage books are included. We excluded all non-single name credit derivatives (e.g. ABX, TABX, CDX, TRS, baskets, CLNs and non-USD hedges and hedges for non-US securities, and positions with zero notional.

Note: We also excluded positions labeled by Bear Stearns with "see confirm" (these files had incomplete information)

Section 4. Single name CDS

US dollar denominated, investment grade single name or pay-as-you-go CDS positions (whether against an investment grade underlying or not) are eligible. Excludes 7 CMDS, which are effectively synthetic CDO baskets, not CDS on CDOs)

These are allocated to the LLC according to the following set of rules:

1. Start with the universe of single name CDS trades from Swap/Derivclear.
2. Remove Duke XI synthetic CDO (but for the avoidance of doubt, any hedges are otherwise eligible)
3. Remove CDMK and KCDM books. Note: BSC identified these as Prime Brokerage books and further data review showed a net exposure of effectively zero
4. Remove exact pairs[9] (i.e., same CUSIP, same coupon, same trading book[10], and same absolute value of notional)
5. Drop "same trading book"[11] restriction and continue removing exact pairs[12]

---

[9] "Pair" comprises one long position and one short position
[10] "Same trading book" are positions held within a discreet sub-book within the Bear Stearns Mortgage desk.
[11] Removing the "same trade book" restriction widens the eligible set of positions screened for exact pairs
[12] Note: Exact pairs referencing two bonds (IXIS and ICM) were not initially recognized as pairs due to errors in certain BSC data. These errors were subsequently corrected and these pairs were removed later in the demarcation process.

6. Keep cusip and coupon restrictions but loosen "absolute value of notional" restriction by removing exact pairs if:

   ***Long's** Absolute Value of Notional minus **Short's** Absolute Value of Notional is between -$10,000 and $10,000.*

   In other words, if Long's and Short's absolute values of notional are within $10,000 of each other, then exclude

7. Remove coupon restriction but add back trading book restriction (i.e., remove exact pairs with same CUSIP, same trading book, and same notional value within $10,000).

8. Drop all restrictions except CUSIP and sum notional values of all hedges sharing one CUSIP. For each CUSIP where summed notional value is less than $1 Million, exclude all hedges with that CUSIP.

9. Remaining hedges are eligible for the Fed facility and will be split as follows:
   - Investment Grade: all positions are included
   - Non-Investment Grade: 40% of positions were included

Note: after this methodology was applied, 16 additional CDS were excluded due to confirmation issues. The exclusion of these CDS was applied after the CMBX amount (below) was applied. As a result, the total CDS plus CMBX exposure assigned to the LLC was less than the targeted $3.7 BN.

Section 5. CMBX

Eligible universe: any US dollar denominated CMBX position

CMBX inclusion was not determined based solely on eligibility, but also on the size of the CDS portfolio: CMBX was added to the portfolio to make the total amount of upfront premiums on CDS plus CMBX equal to $3.7 BN.
- CMBX 'target' was determined by subtracting the total amount of upfront premium on eligible CDS from $3.7 BN
- All eligible CMBX were included: While the BSC portfolio included many line items of CMBX, there existed only 26 distinct exposures (by series and rating). Therefore, those CMBX representing the same exposures were netted and collapsed into 26 distinct exposures for the purposes of the demarcation.
- Each of the 26 net exposures were split in equal proportion in order to match the target amount (i.e. by the ratio target notional/total eligible notional).
- CMBX notionals were rounded to the nearest $1M

- Once the total exposure eligible for the LLC was calculated, 26 new trades were created to match the 26 positions to be transferred into the LLC (this approach was used because the existing positions in the BSC portfolio could not easily be 'split' to precisely match the position sizes eligible for the LLC)

Section 6. Non-credit hedges

The following types of non-credit hedges are in scope:

- Futures, Options on Futures
- Steepener/curve trades as defined by the documentation provided by Bear Stearns on 3/20/2008 12:35 pm
- Treasuries
- Swaps - note that we have taken the swaps that were initially designated as matured. These were not really matured but were terminated on 3/25.
- Equity Options
- Equity Shorts
- TBA, unless proven to be associated with an asset that is excluded from the Fed book or unless non-investment grade

Demarcation rules:

- Equity IYR short is not included due to lack of documents
- Steepener, equity options and equity shorts were split between the FRB-NY and JPM in a ratio of 61.9%/38.1% respectively[13]. This was based on a verbal agreement between FRBNY, JPM and BLK on March 18, 2008. This decision was made earlier than other demarcation decisions due to the urgency of the trade on these positions.
- Treasuries, futures, and options on futures were split based on DA Desk[14] pop analysis[15] and negotiations based on whether related assets were being transferred to FRB-NY.
- TBAs and Swaps were split purely based on negotiations looking at DA Desk and assets going to JP/Fed.

---

[13] Result was rounded to the nearest $1 MM

[14] DA Desk is a term used in BSC's front end systems to identify sub-desks of the BSC mortgage desk

[15] I.e. "Pops" are a form of DV01 value. BLK and JPM reviewed the pops of the securities being allocated to FRB-NY vs. JPM. Hedges were split based on these pops.

Note:

Where a security or loan was traded without the approval of BLK or FRB-NY after March 14 but prior to the close of the facility, the Fed reserved the right to put these securities back at the March 14 market value rather than receive (in the post close true up) the proceeds from the trade.