COUNTERPARTY RISK MANAGEMENT POLICY GROUP II

July 25, 2005

Mr. Henry M. Paulson, Jr.
Chairman and Chief Executive Officer
Goldman, Sachs & Co.
85 Broad Street
New York, NY 10004

Dear Hank:

On behalf of the Counterparty Risk Management Policy Group II, I am pleased to convey to you our Report entitled *Toward Greater Financial Stability: A Private Sector Perspective,* dated July 27, 2005. As you will readily observe, the Report is a broad and far-reaching effort aimed primarily at further strengthening the stability of the global financial system. The scope and reach of the Report is a great tribute to the Members of the Policy Group. Their efforts have been truly extraordinary not only in terms of the rigor and quality of their work but, more importantly, in the statesmanship they displayed in their willingness to put aside narrow interests in order to produce a Report that unquestionably serves the public interest. In that regard, I want to express to you my sincere gratitude for the time and effort devoted to this project by Craig Broderick who served as a Member of the Policy Group and the others from Goldman Sachs who participated in the project and are named in the Report.

The Report itself — building on the 1999 work of Counterparty Risk Management Policy Group I — is directed at initiatives that will further reduce the risks of systemic financial shocks and limit their damage when, rarely but inevitably, such shocks occur. The context of the Report is today's highly complex and tightly interconnected global financial system. The Report's Recommendations and Guiding Principles focus particular attention on risk management, risk monitoring and enhanced transparency.

In addition, the Report covers a number of related areas including: (1) strengthening the infrastructure of the financial system; (2) in the context of complex products, better defining the respective roles and responsibilities of financial intermediaries and their institutional clients; (3) suitability standards for the sale of complex products to retail investors; (4) the management of potential conflicts of interest; and (5) the changing risk management challenges facing institutional fiduciaries. Finally, and of great importance, the Report also examines in considerable detail the challenges faced by market participants with regard to the management and use of highly complex financial instruments.

While much of the Report is directed at well-known categories of financial risk, a great deal of attention is also focused on operational and reputational risks. This emphasis on operational and reputational risks reflects the hard reality that these elements of risk are critically important ingredients to sustaining public confidence in the financial system. As such they are highly relevant to the goal of financial stability.

Many of the Report's Recommendations and Guiding Principles are enhancements and refinements of initiatives already underway across the financial system. However, even where this is the case, the enhancements and refinements are substantive and material. Needless to say, these measures are a complement to — and not a substitute for — various laws and regulations in jurisdictions around the world.

The Policy Group views its Recommendations and Guiding Principles as a forward-looking and integrated framework of initiatives. They are written in a manner that should make it straightforward for senior management, auditors, boards of directors and regulators to track the progress individual institutions are making relative to these standards. The Report also repeatedly stresses that while the initiatives outlined in the Report are central to the goal of financial stability, they are by no means substitutes for the overriding importance of the time-honored basics of managerial competence, sound judgment, common sense and the presence of a highly-disciplined system of corporate governance. Indeed, these basics are key ingredients to building and sustaining a culture in which reputational excellence and commercial excellence can thrive side-by-side.

Most of the Recommendations and Guiding Principles relate to measures that are within the control and reach of individual institutions. Others entail collective actions by institutions and their so-called "trade groups." In that latter category, I want to call your particular attention to Recommendations 12, 21 and 22, which call for urgent industry-wide efforts (1) to cope with serious "back-office" and potential settlement problems in the credit default swap market and (2) to stop the practice whereby some market participants "assign" their side of a trade to another institution without the consent of the original counterparty to the trade. Among other things, this practice has the potential to distort the ability of individual institutions to effectively monitor and control their counterparty credit exposures.

I should also note that in the course of its deliberations, the Policy Group met twice with a group of about one dozen representatives of supervisory and regulatory bodies from various parts of the world. The purpose of these informal meetings was to keep these officials informed of the progress of our work and to share with them the broad thrust of our Recommendations and Guiding Principles. It was clearly understood by all at the outset that these individuals were not representing nor speaking on behalf of their employers and that neither the individuals nor their employing agencies were being asked to endorse the Report or any of its component parts.

In closing I want to emphasize that the Policy Group believes that senior management of individual financial institutions should ensure that such institutions review the Recommendations and Guiding Principles contained in this Report and, where appropriate, take steps to bring their business practices into line with these standards.

Sincerely,

E. Gerald Corrigan

Please note: virtually identical letters have been sent to the Chief Executive Officers (or their equivalents) of all of the institutions having members on the Policy Group.