



Memo

To: The MDE Clients
From: The MDE Group, Inc.
Date: September 29, 2008
Re: Safety and Stability of Client Assets

The safety of your money is of paramount importance to all of us at The MDE Group. With careful thought and foresight we selected Charles Schwab, Fidelity, and The Bank of New York to act as custodian for our client assets. We selected these firms because of their financial strength, significant experience, and stable business models. **Table 1** below shows selected metrics illustrating the strength of MDE's custodians.

Table 1: Financial Strength of The MDE Group's Custodians

Measure of Strength	Schwab	Fidelity	Bank of NY
Revenues (2007)	\$5.3 Billion	\$14.9 Billion	\$14.5 Billion
Profits (2007)	\$1.3 Billion	\$2.2 Billion	\$2.4 Billion
Excess Insurance	\$600 Million	Unlimited *	Unlimited *
Assets **	\$1.4 Trillion	\$3.2 Trillion	\$23.0 Trillion
Year Founded	1971	1949	1784

* Unlimited refers to protection for the total net equity in the account
** Includes assets under management and custody

The rapid downfall of Bear Stearns and Lehman Brothers had much to do with the business model of those firms. They were reliant on short-term funding from other financial institutions, and their assets were primarily long-term in nature. Accordingly, once financial firms began to mistrust each other, short-term funding became scarce and eventually evaporated for firms with exposure to toxic mortgage backed securities. The long-term assets of Bear Stearns and Lehman Brothers could not be liquidated quickly and at fair market values, hence the threat or realization of bankruptcy for these firms.

Conversely, Charles Schwab, Fidelity, and The Bank of New York do not rely on short-term funding from other financial institutions in order to operate their businesses. The Bank of New York relies in part on stable customer deposits to finance its activities and has access to the Federal Reserve Bank in the event of a liquidity squeeze. Charles Schwab has a relatively low Debt to Equity ratio of 0.2 (vs. 20:1 or more for traditional Wall Street investment banks) and more than \$600 million in freely available cash. Fidelity is a privately held company that does not fully disclose its financials, but its business does not rely on debt in order to fund its operations. In short,

it is highly improbable that the issues that resulted in the downfall of Bear Stearns and Lehman Brothers can occur with Charles Schwab, Fidelity, and The Bank of New York.

In the unlikely event of a bankruptcy, all financial institutions have procedures in place designed to safeguard client assets. First, it should be noted that most securities are held with the Depository Trust Corporation (DTC). According to DTC rules, clients have full right to securities which are held at DTC and creditors have *no access* to these securities. However, custodians often lend out customer securities which may make the simple process of returning securities to investors somewhat complex. Therefore, we believe it would be helpful to discuss in further detail the sequence of events post bankruptcy.

Once a securities firm declares bankruptcy, a trustee or receiver is appointed by the federal court to act as steward for the distressed firm's assets. The trustee then transfers the accounts of the bankrupt firm to another (solvent) member. Securities are then matched to their appropriate owners. If securities are missing or are in lesser amounts than expected, a (pre-insurance) loss occurs. The Securities Investor Protection Corporation (SIPC) provides insurance coverage designed to satisfy any remaining claims up to \$500,000 per client, of which \$100,000 may be claims for cash. If this insurance is insufficient, most firms maintain "excess insurance" that is designed to cover additional losses. For example, Charles Schwab maintains \$600 million in excess insurance, with a maximum value of \$150 million awarded to a single client. On the surface, \$600 million in coverage for a firm with more than \$1 trillion in assets may seem insufficient. However, the two layers of insurance cover securities that cannot be located or were misappropriated. The magnitude of these errors has traditionally been very small on a percentage basis and well covered by excess insurance policies.

There have been 317 failures of broker-dealers since 1971. The SIPC, and excess insurance held by each firm, recovered more than 99.95% of assets, subsequent to the broker-dealer bankruptcy. Any losses in excess of insurance are shared on a pro-rata basis among all clients of the failed financial institution. Therefore, actual dollar losses have historically been minimal. In some cases of historical default, there have been delays in clients obtaining access to their securities. Christopher Cox, Chairman of the Securities and Exchange Commission (SEC), had the following to say about the safety of client assets held at Bear Stearns:

"Despite the run on the bank to which Bear Stearns was subjected, its customers were fully protected. At no time...were any of the customers of Bear Stearns's broker-dealer at risk of losing their cash or their securities."

In sum, MDE feels highly confident in the safety and stability of the funds that you have entrusted to us and we continuously monitor the creditworthiness of all the financial institutions that we transact with. If you have any questions related to the safety of your assets, we would be pleased to answer.