

LB UK RE Holdings Limited – In Administration

Joint Administrators' progress report for the period 15
September 2008 to 14 March 2009

9 April 2009

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Section 1: Purpose of the Joint Administrators' progress report

Introduction

In accordance with Rule 2.47 of the Insolvency Rules 1986 ("IR86"), the Joint Administrators (the "Administrators") write to provide creditors with details of the progress of the Administration of LB UK RE Holdings Limited (the "Company" or "LB UK RE") for the six months since the Administrators' appointment on 15 September 2009.

Adoption of the Administrators' proposals

On 4 November 2008 the Administrators circulated to all known creditors their proposals for achieving the purpose of this Administration (the "Proposals"). The Proposals were approved by creditors at a meeting held on 20 November 2009.

Creditors' Committee

A Creditors' Committee was formally constituted on 29 January 2009 and consists of the following members:

1. Eldon Street Holdings Limited
2. Reed Smith Richards Butler LLP
3. Lehman Brothers Europe ("LBEL")
4. Lehman Brothers Holdings Inc ("LBHI")
5. Lehman Brothers Limited ("LBL")

The Administrators are liaising with the Creditors' Committee to discuss significant issues and outline key decisions. The Administrators met with the Committee on 11 March 2009.

Outcome for creditors

At this time the Administrators are unable to provide a reliable estimate of the likely dividend to creditors as there are material uncertainties regarding future net realisations and the final level of creditor claims. These matters are discussed in this report.

What steps should be taken now

The Administrators will continue to manage the Administration in accordance with the Proposals approved by creditors and in consultation with the Creditors' Committee.

Until there is more certainty regarding dividend prospects, claims agreement work will be restricted to gathering information. If you have not already submitted your claim to the Joint Administrators, please do so by completing and returning the attached statement of claim form.

Future reports

The Administrators will next report to creditors in approximately six months.



D Y Schwarzmann
Joint Administrator
LB UK RE Holdings Limited

Section 2: Background information

Background information

Investment banking was at the core of the business of the global Lehman Brothers Group of companies (the “Lehman Group”). Until its recent collapse the Lehman Group provided financial services to corporations, governments, municipalities, institutional clients and high net worth individuals.

The ultimate parent company of the Lehman Group is LBHI, which is incorporated in the United States of America.

LBHI centrally managed substantially all of the material cash resources of the Lehman Group.

In the period immediately prior to its insolvency there was an escalating loss of confidence in the Lehman Group. This was evidenced by a significant deterioration in LBHI’s share price on the New York Stock Exchange of almost 80 per cent during the week from Friday 5 September 2008 to Friday 12 September 2008.

On Wednesday 10 September 2008, the Lehman Group announced a third quarter loss of US\$3.9 billion. At the same time, the Lehman Group announced plans to sell a majority stake in its investment management business and to spin-off the majority of its commercial real estate assets into a new, separate public company. These measures failed to restore investor confidence and the share price fell by 7 per cent on the same day.

During the afternoon of 14 September 2008, we met with the directors of Lehman Brothers International (Europe) in order to consider what steps should be taken in the event that discussions to save the Lehman Group were to fail. A continuing failure of LBHI to settle obligations on behalf of LB UK RE at any point in time would result in the insolvency of LB UK RE, as it would be unable to meet its liabilities as they fell due.

At approximately 12.30 am on 15 September 2008, LB UK RE was informed by LBHI that it would no longer be in a position to make payments to or for LB UK RE and other Lehman Group companies and was preparing to file for Chapter 11 bankruptcy protection in the US.

Overnight, preparations were made by the directors, employees and advisers for a number of the Lehman Group companies in the UK to seek the protection of administration orders and directors of those companies, including LB UK RE, met and resolved to place those companies into Administration (collectively “the Lehman Administration Companies”).

At 7.56 a.m on 15 September 2008, Administration orders were made in respect of each of the Lehman Administration Companies. Immediately upon their appointment the Administrators and their teams assumed responsibility for LB UK RE’s affairs and began to pursue the purpose of the appointment. Later on 15 September 2008, LBHI announced that it had filed for Chapter 11 bankruptcy protection in the US.

Section 3: Joint Administrators' actions to date

Objective of the Administration

As it was not reasonably practicable to rescue LB UK RE as a going concern, the Administrators are pursuing the objective of achieving a better result for LB UK RE's creditors as a whole than would be likely if LB UK RE were wound up (without first being in Administration).

Business Activities

The principal activity of LB UK RE was the management of sole and joint venture investments in portfolios of performing, sub-performing and non-performing loans, as well as real estate.

LB UK RE utilised employees seconded from LBL, another Lehman Administration Company and operated from the Lehman Group's premises at 25 Bank Street, London E14 5LE.

Summary of actions taken to date

Following the approval of their Proposals on 21 November 2008, the Administrators have focussed on:

- protecting and managing LB UK RE's assets; and
- realising these assets in an orderly manner.

The following sections summarise the work that has been carried out by the Administrators and their staff in respect of LB UK RE's principal assets.

Section 3.1: Loan portfolios

Background

LB UK RE invested in portfolios of sub and non-performing loans (“SNPLs”) throughout the world. These SNPL portfolios comprise a mixture of unsecured loans and loans secured on residential property assets.

LB UK RE’s SNPL portfolios had a total unpaid principal balance (“UPB”) of approximately €2.1bn as at the date of Administration but were acquired at a significant discount to this UPB.

The most significant SNPL portfolios are as follows:

- secured and unsecured loans in Portugal with a total UPB of €570m and a captive loan servicer;
- Polish unsecured loans with a total UPB of €459m, serviced by a third party loan servicer; and
- mortgage backed securities in Germany with a UPB of €485m (the ownership of which are currently under dispute).

Initial strategy

In the absence of prior knowledge of the business activities of LB UK RE, the Administrators:

- developed a comprehensive understanding of LB UK RE’s SNPL portfolios;
- put in place the necessary processes and resources infrastructure to manage the SNPL portfolios on a day to day basis in the context of the Administration; and
- developed and implemented a strategy to maximise realisations from the SNPL portfolios.

In implementing their strategy the Administrators had to overcome significant issues. For example, the Administrators and their legal advisors had to assert their rights over LB UK RE’s assets in territories that were not familiar with the implications of Administration.

Progress since 21 November 2008

Following the approval of the Proposals on 21 November 2008 the Administrators have:

- completed due diligence reviews (financial and legal) of all LB UK RE loan portfolios;
- contacted all significant counterparties and advised them of the Administration, its objectives and strategies;
- secured cash-flows from the SNPL portfolios wherever possible;
- undertaken valuations of the SNPL portfolios;
- developed internal processes for the ongoing run off of the SNPL portfolios wherever the valuation to hold the portfolios was greater than the estimated sale price;
- offered six of the SNPL portfolios to the market through formal or summary sales processes; and
- realised proceeds of approximately \$54m to date through SNPL portfolio sales.

Outstanding matters

The Administrators will continue to:

- manage the SNPL portfolios;
- liaise with servicers, paying agents, correspondent banks and internal treasury to control cash-flows; and
- subject to the overall strategy of the Administration place these assets on the market when they believe realisations can be maximised, mindful of holding costs.

Section 3.2: Real estate investments

Background

LB UK RE was the principal vehicle through which the Lehman Group's European real estate investments were made.

These investments were principally in the form of debt / equity positions in approximately 50 joint venture property holding companies ("JVs") with approximately 40 different partners.

Initial strategy

In the absence of prior knowledge of the business activities of LB UK RE the Administrators:

- quickly developed a comprehensive understanding of LB UK RE's real estate investment portfolio with the assistance of Lehman Group employees and JV partners;
- engaged with JV partners and senior lenders to understand and manage potential defaults or breaches of covenant;
- put in place the necessary processes and resources to manage the real estate investment portfolio on a day to day basis; and
- developed and implemented a strategy to maximise realisations from the real estate investment portfolio.

Progress since 21 November 2008

Following the approval of the Proposals on 21 November 2008 the Administrators have:

- completed a due diligence review of the investment portfolio to determine ownership and servicing requirements;
- instructed independent surveyors to value the underlying real estate assets in locations throughout Europe;
- commenced a formal marketing process for seven real estate investments;
- realised \$2.4 million to date through the sale of investments to two JV partners;

- opened negotiations with six other JV partners for the sale of additional investments; and
- established an in-house loan and asset servicing platform in place of the external provider in order to reduce costs and enhance control.

Outstanding matters

The Administrators will continue to:

- manage the real estate investment portfolio, limiting any losses that may arise as a result of defaults or breaches of covenant (particularly in respect of loan to value covenants); and
- subject to the overall strategy of the Administration place these assets on the market when they believe realisations can be maximised, mindful of holding costs.

Section 3.3: Other investments

Background

LB UK RE's other investments include:

- seed capital investments in Lehman Group funds;
- external hedge fund investments;
- listed company investments; and
- minority stake holdings.

Initial strategy

Immediately upon their appointment, the Administrators and their staff worked closely with Lehman Group employees to:

- understand the legal and beneficial ownership structures of these investments; and
- formulate realisation and retention strategies for each investment, mindful of the prevailing market conditions.

Progress since 21 November 2008

Following the approval of their Proposals on 21 November 2008, the Administrators have made significant realisations in the following categories:

- **Seed capital investments:** Some Lehman Brothers Asset Management funds, in which LB UK RE had invested approximately \$35m, have been wound down realising \$31.4m.
- **External hedge funds:** A \$100m investment and Asset Backed Securities fund has been realised in full and half of a \$50m investment in a Multi-Strategy fund has yielded \$20m in cash (the remainder being redeemed in specie due to market conditions).
- **Minority stakeholdings:** The Administrators have realised \$187m in respect of LB UK RE's 37.8% interest in an investment. A sale contract for this interest had been entered into by LB UK RE prior to the Administration but required significant work to complete at the agreed sale price in a deteriorating market background.

Outstanding matters

The Administrators will continue to:

- retain control of and manage these investments; and
- expedite further realisations that remain dependent on other parties.

Section 4: Statutory and other information

Court details for the Administration:	High Court of Justice, Chancery Division, Companies Court - case 7944 of 2008
Full name:	LB UK RE Holdings Limited
Trading name:	LB UK RE Holdings Limited
Registered number:	05347966
Registered address:	25 Bank Street, London E14 5LE
Company directors:	JC Blakemore, D Gibb, PEJ Hansell, IM Jameson, GR Moar, CJ Patrick, B Porter, AJ Rush and PA Sherwood
Company secretary:	P Dave and ESE Upton
Shareholdings held by the directors and secretary:	None of the directors own shares in LB UK RE
Date of the Administration appointment:	15 September 2008
Administrators' names and addresses:	AV Lomas, SA Pearson, DY Schwarzmann, MJA Jervis and GH Martin, of PricewaterhouseCoopers LLP, Plumtree Court, London EC4A 4HT
Appointer's name and address:	High Court of Justice, Chancery Division, Companies Court
Objective being pursued by the Administrators:	Achieving a better result for LB UK RE's creditors as a whole than would be likely if LB UK RE were wound up (without first being in Administration)
Division of the Administrators' responsibilities:	In relation to paragraph 100(2) Sch.B1 IA86, during the period for which the Administration is in force, any act required or authorised under any enactment to be done by any or all of the Joint Administrators may be done by any or one or more of the persons for the time being holding that office.
Proposed end of the Administration:	The Administrators are not yet in a position to determine the most likely exit route from the Administration and wish to retain the options available to them.
Estimated dividend for unsecured creditors:	It is too early to estimate the likely dividend for unsecured creditors.
Estimated values of the prescribed part and LB UK RE's net property:	There may be sufficient net property to enable a distribution for unsecured creditors under the prescribed but the estimated value of LB UK RE's net property is uncertain.
Whether and why the Administrators intend to apply to court under Section 176A(5) IA86:	It is too early to decide whether such an application might be necessary.
The European Regulation on Insolvency Proceedings (Council Regulation(EC) No. 1346/2000 of 29 May 2000):	The European Regulation on Insolvency Proceedings applies to this Administration and these are the main proceedings.

Section 5: Financial information

Statement of Affairs

The Directors provided the Statement of Affairs on 16 February 2009. This Statement is not attached to the progress report as disclosure of the information therein may impact adversely upon future realisations.

Administrators' remuneration

By way of context, the manner in which Administrators' remuneration is determined and approved is set out in the Insolvency Rules 1986 2.106 to 2.109 (the "Rules").

On 29 January 2009 a Creditors' Committee was formed, whose duties include approving the basis and quantum of the Administrators' remuneration.

There are two alternative bases of determining the remuneration under the Rules, either:

- A percentage of the value of the property with which the Administrator has to deal; or
- By reference to the time properly given by the Insolvency Practitioner and his staff in attending to matters arising in the Administration.

The Rules also provide that in arriving at its decision on remuneration the Committee is required to consider the following matters:

- The complexity (or otherwise) of the case;
- Any responsibility of an exceptional kind or degree which falls on the Administrators;
- The effectiveness with which the Administrators appear to be carrying out, or have carried out, their duties; and
- The value and nature of the property which the Administrators have to deal with.

Statement of Insolvency Practice No.9 ("SIP 9")

In addition to the Rules, SIP 9, issued by the Joint Insolvency Committee provides guidance to insolvency practitioners and creditors' committees in relation to the remuneration of, *inter alia*, Administrators.

The purpose of SIP 9 is to:

- Ensure that Administrators are familiar with the statutory provisions relating to office holders' remuneration;
- Set out best practice with regard to the observance of the statutory provisions;
- Set out best practice with regard to the provision of information to those responsible for the approval of remuneration to enable them to exercise their rights under the insolvency legislation; and
- Set out best practice with regard to the disclosure and drawing of disbursements.

Committee members have each been provided with a copy of SIP 9.

When seeking agreement for remuneration, the Administrators' are required to provide sufficient supporting information to enable those responsible for approving their remuneration ('the approving body') to form a judgement as to whether the proposed remuneration is reasonable having regard to all the circumstances of the case. The nature and extent of the supporting information which should be provided will depend upon:

- The nature of the approval being sought;
- The stage during the Administration of the case at which it is being sought; and
- The size and complexity of the case.

Remuneration review and approval process

In accordance with SIP 9 the Committee has been provided with details of the charge-out rates for all grades of staff which are involved on the case.

As the Administrators' remuneration request is based on time costs the Committee has been provided with an account of the time spent and the charge-out value, together with additional information setting out the approach to the project, the milestones and progress against such milestones.

Given the size and complexity of the case these disclosures have been extensive. This additional information which has been provided comprises an extensive explanation of the Administrators' activities, methods and achievements in order to enable the value of the exercise to be understood.

The time analysis provided to the Committee gives details of the work performed and grade of staff, by Activity, Cross Functional Workstream and Function for monthly periods.

SIP 9 guidance suggests the following areas of activity as a basis for the analysis of time spent:

- Administration and planning
- Investigations
- Realisation of assets
- Trading
- Creditors
- Any other case-specific matters

The analysis that has been provided to the Committee contains 17 subdivisions of time spent.

The following categories are suggested by SIP9 as a basis for analysis by grade of staff:

- Partner
- Manager
- Other senior professionals
- Assistants and support staff

The Committee has been provided with an analysis of staff allocated between six grades.

SIP 9 also suggests that an explanation of what has been done should include an outline of the nature of the assignment and the Administrator's own initial assessment, including the anticipated return to creditors. To the extent applicable it should also explain:

- Any significant aspects of the case, particularly those that affect the amount of time spent;
- The reasons for subsequent changes in strategy;
- Any comments on any figures in the summary of time being spent accompanying the request the Administrator wishes to make;
- The steps taken to establish the views of creditors, particularly in relation to agreeing the strategy for the assignment, budgeting,

time recording, fee drawing or remuneration agreement; and

- Details of how other professionals, including subcontractors, were chosen, how they were contracted to be paid, and what steps have been taken to review their fees.

Each of these matters has been covered in some detail in the discussions we have had with the Committee. The administrative matters referred to in summary in the body of this report have been covered in extensive detail with the Committee and each area of our activities discussed in depth.

Resolution of the Creditors' Committee

The Administrators' remuneration request was made to the Creditors' Committee on 11 March 2009 and its response is awaited.

Receipts and payments account

An account of the receipts and payments in the Administration for the six months to 14 March 2009 is set out in section 6 to this report.

Significant receipts in the period covered by this report include:

- \$5.1m in respect of the sale of real estate investments (including \$2.4m from investments sold to two JV partners);
- \$53.7m in respect of income from and the sale of SNPL portfolios; and
- \$339.3m in respect of income from and sales of seed capital investments, external hedge funds and minority stakeholdings.

Significant payments include:

- building and occupancy costs of \$1.4m;
- payroll and employee costs of \$3.2m;
- legal fees of \$0.7m; and
- insurance premiums of \$1.6m.

Net receipts as at 14 March 2009 total \$389.8m.

Section 6: Receipts and payments

	GBP £	EUR €	USD \$	As at 14 Mar 2009 Total (USD \$)
	mil	mil	mil	mil
Receipts				
SNPL	0.4	15.4	33.5	53.7
Real estate	2.6	1.1	0.1	5.1
Seed capital investments	-	1.0	30.1	31.4
External hedge funds	0.2	-	120.2	120.4
Minority stakeholdings	-	147.6	0.1	187.5
Internal currency transfer	3.7	-	-	5.3
Total receipts for period	6.9	165.1	184.0	403.4
Payments				
Building and occupancy cost	1.0	-	-	1.4
Payroll and employee costs	2.2	-	-	3.2
Legal fees	0.5	-	-	0.7
Insurance	1.1	-	-	1.6
Principal investments	-	-	0.3	0.3
Professional fees	0.3	0.4	-	0.9
Real estate valuations	0.1	-	-	0.1
Internal currency transfer	-	0.7	4.6	5.4
Total payments for period	5.2	1.1	4.9	13.6
Net receipts	1.7	164.0	179.1	389.8
Held as				
BoE	0.1	4.8	35.7	41.9
HSBC	1.6	19.1	98.4	125.0
Money markets	-	140.1	45.0	222.9
Total cash	1.7	164.0	179.1	389.8

USD \$ equivalent is for information purposes only.
Rates used for conversion are Financial Times rates
on 14 Feb 2009:

1 GBP £ = 1.4254 USD \$
1 Euro € = 1.2701 USD \$