Lehman Brothers Limited – In Administration

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

14 April 2009

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Section 1: Purpose of the Joint Administrators' progress report

Introduction

This report has been prepared by the Joint Administrators of Lehman Brothers Limited ("LBL" or the "Company") under Rule 2.47(3)(a) of the Insolvency Rules 1986.

Creditors were notified of the Joint Administrators' Proposals for achieving the purpose of the Administration on 5 November 2008. These were approved at a meeting of creditors held on 21 November 2008.

This report provides details of the work undertaken and the progress made during the first six months to 14 March 2009.

Objectives of the Administration

The Joint Administrators are pursuing the objective of achieving a better result for LBL's creditors as a whole than would be likely if LBL were wound up (without first being in Administration).

The specific aims of this Administration are to:

- Realise all assets of LBL, where value may exist;
- Provide ongoing employee and infrastructure support to the other group companies that are in Administration in exchange for appropriate reimbursement; and
- Mitigate, as far as possible, any further liabilities against LBL by the transfer or termination of contracts.

Creditors' Committee

Your Creditors' Committee (the "Committee") was elected at the meeting of creditors and its members are:

1. Lehman Brothers Holdings Inc
2. The Trustees of the Lehman Brothers Pension Scheme
3. Heron Quays (HQ2) T1 Limited
4. Origin HR Consulting Limited.

The Joint Administrators meet with the Committee regularly. To date, three meetings of the Committee have taken place.

The meetings with the Committee provide the Administrators with the opportunity to explain in detail how we are dealing with key aspects of the Administration and to consult with them on critical issues.

Outcome for unsecured creditors

The Joint Administrators are not in a position to give an estimate of the timing or quantum of any dividend to unsecured creditors.

However, creditors should be aware that LBL is a shareholder of Lehman Brothers International (Europe) – in Administration, an unlimited company. LBL is therefore potentially liable for any shortfall to creditors of that estate. This could clearly have a significant impact on funds available to creditors of LBL.

Future reports

The next progress report to creditors will be in six months time.

Signed:

MJA Jervis
Joint Administrator
Lehman Brothers 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 was one of the four biggest investment banks in the United States. It provided financial services to corporations, governments and municipalities, institutional clients and high net worth individuals. The business activities of the Lehman Group were organised in three segments, namely: capital markets, investment banking and investment management. Those segments included businesses in equity and fixed income sales, trading and research, investment banking, asset management, private investment management and private equity.

The Lehman Group's headquarters were in New York, with regional headquarters in London and Tokyo and many offices in North America, Europe, the Middle East, Latin America and the Asia-Pacific region.

The ultimate parent company of the Lehman Group is Lehman Brothers Holdings Inc. ("LBHI"), which is incorporated in the United States. The main trading companies within the UK were Lehman Brothers International (Europe) ("LBIE") and Lehman Brothers Europe Limited ("LBEL").

Events immediately preceding the Administrators' appointment

The Lehman Group operated in a market that depends heavily on investor and market confidence. In the period immediately prior to its insolvency, there was an escalating loss of confidence in the Lehman Group, as 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 Tuesday 9 September 2008, the share price fell 45 per cent following reports that negotiations with the Korean Development Bank, regarding a potential major investment in the Lehman Group, had been put on hold.

The following day, 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 a further 7 per cent on Wednesday 10 September 2008.

Following the close of business that day, Moody's Investors Service, one of the main credit rating agencies, announced that, in the absence of a purchaser for the Lehman Group or its business by Monday 15 September 2008, it intended to downgrade the Lehman Group's credit rating.

Various steps were taken in an attempt to resolve the Lehman Group's situation. We understand that weekend discussions were held in New York with potential investors and purchasers of the Lehman Group's business (or part thereof).

During the afternoon of 14 September 2008, we met with the directors of LBL in order to consider what steps should be taken in the event that the New York discussions to save the group were to fail.

LBHI managed substantially all of the material cash resources of the Lehman Group centrally. A continuing failure of LBHI to settle obligations to, or on behalf of, LBL at any point in time would result in the insolvency of LBL, as it would be unable to meet its liabilities as they fell due. On 14 September 2008 the directors of LBL sought assurances from LBHI that payments due to be made to LBL on 15 September 2008 would in fact be made by LBHI. The directors also planned how to react in the event that these assurances could no longer be given by LBHI.

LBL was due to pay employee wages on 17th September, and significant rental payments approximately a week later.

At approximately 12.30 am on 15 September 2008, LBL was informed by LBHI that it would no longer be in a position to make payments to or for LBL and other Lehman 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 LBL, met and resolved to place those companies into Administration (collectively "the Lehman Administration Companies").

At 7.56 am on 15 September 2008 Administration Orders were made in respect of each of the Lehman Administration Companies. Having been appointed, the Administrators and their teams immediately assumed responsibility for LBL'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.

Business Activities

LBL was pivotal to the Group's operations as it held most of the UK Group's service contracts including employee contracts. LBL also maintained IT and general infrastructure to support the needs of the Group.

In Administration, LBL has continued to provide services to other Lehman Administration Companies, and to receive cash from other Group entities to cover these costs. LBL has been able to reduce the number, and therefore the value, of creditor claims it will receive.

LBL provided the following to the Lehman Group within the UK:-

Central resources

LBL managed the key operational costs for the Group, including employee wages, rent, rates and utilities. LBL received money to pay these costs from other group companies (including LBIE and LB UK RE Holdings Limited) according to the services provided to each.

Employees

LBL employed the majority of the personnel who worked in the UK trading and operating companies.

LBL also managed secondments and organised all other personnel matters.

Property

The leases for many of the UK Group properties were held by LBL.

Administrative services

LBL organised other administrative needs for the Group including mobile phone, photocopier and computer contracts.

Information Technology

LBL provided IT infrastructure and support to many of the UK Lehman companies.

Section 3: Overview of the actions taken by the Joint Administrators since appointment

As set out in the Administrators' Proposals, dated 5 November 2008, LBL was pivotal to the Group's operations as it held most of the UK Groups' service contracts including employee contracts. LBL also maintained IT and general infrastructure to support the needs of the Group.

In Administration, LBL has continued to provide services to other Lehman Administration Companies, and to receive cash from other Group entities to cover these costs. LBL has been able to reduce the number, and therefore the value, of creditor claims it will receive.

Since their appointment, the Administrators have used specialist teams from within PricewaterhouseCoopers LLP, working with retained LBL employees, to ensure the operations of LBL are properly coordinated and the objective of the Administration is met. The teams are:

- Infrastructure and property
- Recharges
- Information technology
- Human Resources
- Pensions
- Tax
- Intercompany, and
- Affiliate company relationships.

We comment in more detail on the activities of the teams overleaf.

The teams are coordinated and managed by a central Project Management Office (PMO), which is responsible for agreeing the overall team structures and objectives, monitoring progress, and ensuring appropriate resourcing.

On 22 October, the Administrators of LBL, LBIE and other Lehman Administration Companies completed the sale of the Investment Banking, Global Finance and Equity divisions to Nomura. Following this sale:

- The HR team has addressed the legal and practical issues of separating and transferring approximately 2,400 employees;

- The Infrastructure and Property team have addressed the relocation of people within the building (Nomura taking a sublease of part of 25 Bank St), and the identification and recharging of costs; and

- The IT team have addressed consequential IT changes whilst ensuring continuity of services.

A Cost Recharge Agreement has been implemented to enable LBL to recover costs from other Lehman Administration Companies to the extent they are not recovered from other entities, or attributable to LBL's activities on its own behalf.

In addition to ensuring delivery of services to other Lehman Administration Companies, and to recharging and recovering costs incurred, LBL has its own assets, comprising primarily fixtures, fittings, IT assets and tax refunds, as well as inter-company receivables. The teams' responsibilities include the management and realisation of those assets, for the benefit of the creditors of LBL, and the minimisation of obligations to creditors.

Section 3.1: Infrastructure and Property

Background

At the commencement of the Administration, LBL held the service (IT and property) contracts required to support the Lehman Administration Companies, including leases and other contracts for properties and in particular 25 Bank Street (the current location of the bank in the UK), Broadgate (the previous UK headquarters), data centres, business continuity centres, overflow offices, residential properties, European branches and storage facilities.

LBL recovers costs incurred under the relevant leases and contracts from the Lehman Administration Companies and from subtenants of the property at 25 Bank Street.

Objectives

The objectives of the Infrastructure and Property team are to:

- Ensure the delivery of infrastructure and property services;
- Process supplier transactions on behalf of the Lehman Administration Companies;
- Minimise the costs of Infrastructure and Property as far as practicable; and
- Coordinate the recovery of incurred costs on an appropriate basis from the participating entities.

Progress to date

Initial issues

Our priority has been to:

- Identify and retain key LBL employees essential to the management of infrastructure and property;
- Implement controls to ensure costs are authorised by an appropriate team under the control of the Administrators;
- Review the budgeting process to ensure we understand the costs incurred;
- Support the negotiation of cost sharing agreements and to implement a recharge mechanism enabling LBL to recover costs; and
- Negotiate and agree bases for continued supply of services from vendors. To date no critical services have been interrupted. Immediately following our appointment, a number of vendors commenced legal proceedings against LBL for purported breaches of pre-Administration contracts. These disputes have to date been managed without disruption to services.

Properties

London

Negotiations with the landlord of 25 Bank Street, Canary Wharf Group, as a part of the sale of businesses to Nomura, resulted in the sub-letting of approximately one third of the building to Nomura.

25 Bank Street has been reorganised to optimise occupancy efficiency and reduce costs. LBL is looking to market the empty space using its agents.

25 Bank Street has changed from a single tenanted building to a multi tenanted building. Significant effort has been committed to supporting the tenants of the building, including Nomura, which has materially reduced the occupancy and operating costs for the Lehman Administration Companies.

Given the costs and risks associated with being the head lessee for a property such as 25 Bank Street, a major focus has been to identify and implement the best management structure to support the operation of the building. This process is ongoing and meanwhile we have negotiated continuing arrangements with vendors ranging from mail room services through to building maintenance, which both reduce costs and preserve our ability to operate.

Numerous savings have been achieved by reducing contracts with other LBL landlords and service providers, such as the surrender of the lease at Broadgate, and the reduction, transfer or termination of LBL's contracts with business continuity centres and storage facilities.

Branches

Property transfers or disposals have now been completed in Kuwait, Riyadh and Munich.

Future Strategy

The main priority is to assess potential, alternatives to the current infrastructure arrangements. This is a very challenging project, particularly given the IT infrastructure within 25 Bank Street.

These decisions will be explored with the Creditors' Committee over coming months.

Section 3.2: Recharges

Cost Recharge Mechanism

LBL exists as a service company, holding contracts and making payments to employees and suppliers for services that enable the other Lehman Administration Companies to perform their functions, but which are of little benefit to LBL on a standalone basis.

Our priority has been to review LBL's budget and develop a strategy that would enable it to recover these costs. Following this review, we implemented a Cost Recharge Agreement which now provides LBL with a contractual entitlement to recover its outgoings from other group companies.

Under the Cost Recharge Agreement, LBL is reimbursed for payroll costs relating to any employee paid by LBL, who has worked for a group company. The identity of the group company concerned is determined by reference to the objectives that have been agreed with each employee and which refer to the various work-stream activities being undertaken.

To recover building, occupancy and operational costs, which account for all non-payroll costs incurred by LBL, we apportion the total budgeted costs across the group companies, based on the proportion of Lehman Group staff working in 25 Bank Street on behalf of each company. This excludes legal advisors and Administrators' staff who work at 25 Bank Street, however it was agreed that using Lehman Group staff numbers would provide a reasonable indication of the level of activity being carried out in each company. It also avoided the complexities associated with advisory staff working across multiple activities.

We are continuing to refine the model to make the apportionment as fair as possible. The fact that costs for vacant space need to be recharged makes occupation of 25 Bank Street more expensive than market rates; however LBL is committed to recharging all of its costs and, as a service company, we believe that it is reasonable for it to do so.

Since the Administration began we have issued invoices to Lehman Group companies under the Cost Recharge Agreement totalling over £168 million.

Section 3.3: Information Technology

Objective

The objective of the IT function is to provide the Lehman Administration Companies with a secure, stable, cost effective and appropriate technology platform to facilitate the achievement of the purposes of the Administration Orders.

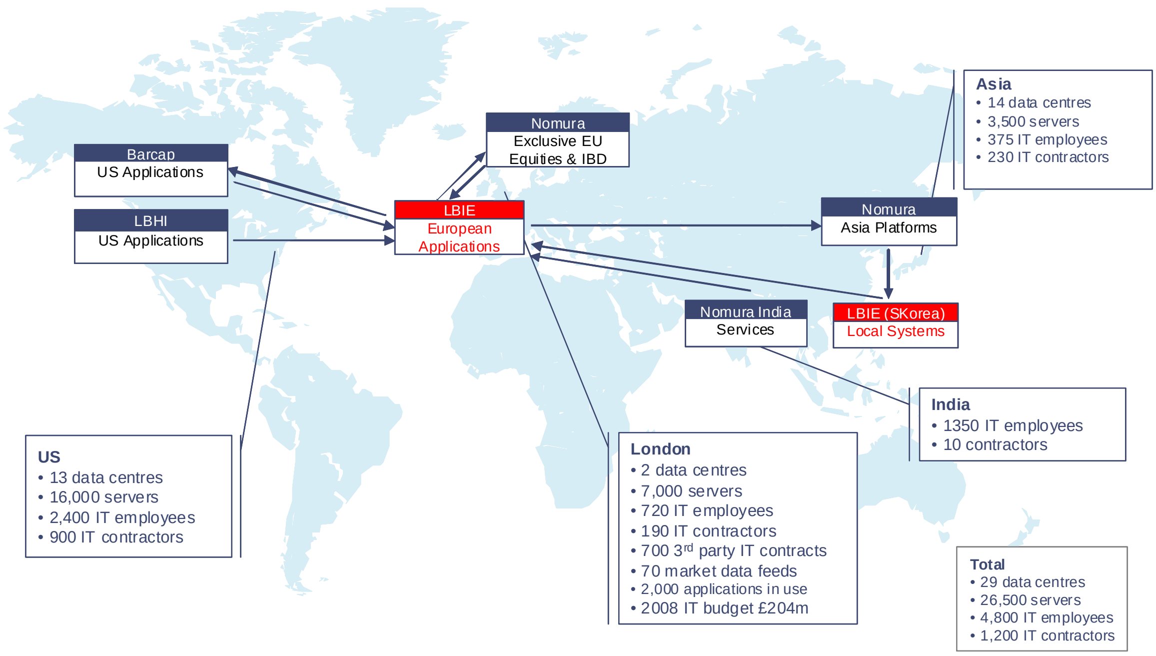
The key tasks are to:

- Refine the technology solution to meet changing requirements over time;
- Minimise the risks represented by dependencies on third parties;
- Manage the service delivery from third party purchasers of businesses;
- Manage key contracts with external parties;
- Decommission the legacy technology in an optimal fashion;
- Capture and store data from the core applications for future use;

Background on the legacy architecture

Similar to most other large investment banking groups, Lehman Brothers operated a global IT architecture that was independent of legal entity. Application developers and support staff were located in London, New York, Sweden, India and the Far East and applications tended to be hosted where the developer that had led the development was based. Development of applications was also shared globally with multiple legal entities contributing development time and funding.

The diagram below illustrates the scale of the IT infrastructure in terms of numbers of staff, applications and the servers that hosted the applications.



The complexity of the architecture led to a number of immediate issues for the Lehman Administration Companies:

- The IT service needed to ensure the wind down of trading positions in the UK had to be provided from multiple locations and legal entities including third party purchasers of the businesses;

- Ownership of the IT infrastructure including the core business applications was not clear; and

- Key data that was needed to unwind the trades was co-mingled with other entities' data and was located in a number of different global locations.

Progress to date

After securing control of and access to key data, applications and infrastructure, we then needed to implement a model to allow us to run IT to support the wind down.

To achieve this we performed the following:

- Gained an understanding of key systems required for the Administrations. As at 15 September 2008 the Lehman Administration Companies were dependent upon over 2000 applications. We analysed and reduced the business requirements and settled on 120 critical applications. This allowed us to start retiring redundant applications;

- Analysed the IT staff for ongoing support – we identified a core number of staff needed to support the IT on an ongoing basis, being 60 core staff out of the original 720. Appropriate cost reductions were implemented and a number of IT staff had, in any event, resigned;

- Implemented an operating model and governance processes for on-going IT support;

- Negotiated a Transitional Service Agreement ("TSA") with a third party purchaser of the main London based investment banking and equities business – this covered IT applications and support that they would provide to us, the infrastructure that we would provide the related costs to be recharged and defined service levels;

- Negotiated a TSA with LBHI to allow mutual provision of services;

- Negotiated a TSA with other third party business purchasers, which is due to be completed over the coming weeks;

- Reviewed contracts for software applications, IT service provision and market data provision, ensuring coverage for those services we needed and terminating those that we did not need;

- Developed and agreed data governance principles with other entities to allow trading data to be passed from co-mingled sources to entities entitled to such data; and

- Identified key data that needed to be archived for forensic and legal purposes and developed a plan for archiving, accessing and interpreting data.

These focussed actions have contributed to a reduction in the cost base for IT for LBL from £204m to approximately £50m.

We now have a secure, stable, cost effective and appropriate technology platform to support wind down activities.

Key issues and challenges

Migration to the target IT architecture

Two of the key tasks to achieve the objective of the IT function are to:

- Refine the technology solution to meet changing wind down requirements over time; and

- Decommission the legacy technology achieving best possible outcome for creditors

We have performed a considerable amount of analysis to asses the options for the target architecture. We considered three key options:

- **Legacy option** - Use existing architecture (fairly complex architecture based in US and Europe) – a number of the applications currently being used are being supported by third parties. The TSAs that allow us access to these applications have a defined end date. In addition, the current infrastructure is reasonably complex and costly with potential for simplification. It was therefore decided that this was not a long term solution.

- **Simplification** – Use a rationalised UK-based architecture and eliminate dependencies by recreating hosted applications in the UK or replacing them with alternative applications. We would also need to take a similar approach for other hosted applications as we neared the end of the TSA.

- **Outsourcing** – Outsource the required application functionality, support and potentially, some business processes to third party service providers leaving only decision making with the Lehman Administration Companies. After investigation it was apparent that the complexity of the infrastructure makes wholesale outsourcing not practical or cost effective.

The strategy for the target IT architecture is a combination of Simplification and Outsourcing. For areas where we can find a suitable third party service provider we will outsource. This can primarily be achieved for front office valuation applications.

For back office applications where we have not yet identified appropriate third party service providers we will migrate a number of the core applications, including the mainframe cash settlement system onto a single application that provides the required functionality.

We are currently running a proof of concept for an application. The application is already owned and we have sufficient in-house IT and operations skills. We will then need a small number of other core middle office and back office applications where the core replacement system does not include that functionality.

Customisation of tools to support the Administration

Since the business processes that are required to perform the wind down differ from the legacy business processes, we have customised the legacy applications to provide tools to support our activities. Key tools that have been customised and are being provided for wind down are:

- **ART (Asset Realisation Tool)** – this provides a single counterparty view that identifies all the exposures to a single counterparty and stores all related counterparty valuations, positions and allows a statement to be prepared, once all data is available

- **The Trust Property Tool** – This tool facilitates the process to capture data from clients with trust property and segregated client money. It interfaces with ART in relation to valuation data.

- **DART (Daily Asset Reporting Tool)** – this tool provides a front end reporting layer for information that is stored in the mainframe settlement system to provide an easier user interface to view a stock's position from books and records and from the external world depots.

- **QMS (Query Management System)** – this system tracks all external queries received and tracks response and resolution.

- **The Creditor Claims database** – this database allows creditors to electronically enter the exposures to Lehman Brothers International (Europe) - in Administration, and their valuations.

Separation of the network

As described above, the legacy IT architecture was global. After business sales to competing organisations, these competing organisations were using the same IT architecture.

In January 2009, we were informed that networks between the UK and US were to be separated. The Lehman Administration Companies need to continue to access the US applications until the migration to the Target Architecture has been achieved. To avoid potentially damaging consequences to the Lehman Administration Companies, a joint working group was formed to manage the separation.

A major project was initiated in January to perform the following:

- Manage the interaction with those third parties required to help support LBL and LBIE during the separation;

- Assess the impact of the separation on the wind down processes;

- Identify where there are potential issues in terms of continued access being required and identify solutions to maintain that access;

- Perform testing of the solutions prior to network separation; and

- Manage the impact of the separation over the separation weekend and the following weeks.

Over 110 people from the IT function, other Administration work streams, activities and functions and TSA providers were involved in the project including 4 weekends of testing.

Network separation was achieved successfully on the weekend of February 21st with minimal impact on the Lehman Administration Companies.

Future priorities for the IT function

Over the next few months, the IT function will be focussed on:

- On-going day to day support of the IT architecture;

- Continued customisation of tools to support the Administration including a tool to track contact with counterparties;

- Management of service from third parties;

- Migration to the target IT architecture

    - Including proof of concept with front office valuation providers

    - Completion of proof of concept with main frame replacement

    - Rationalisation of applications.

- Input into the project to investigate infrastructure options by ensuring that dependency on the in-house data centre is removed.

The accomplishments of the IT Team have been critical to managing the ongoing position and extracting and analysing data. It is likely to require considerable resources over the coming months to preserve functionality and effectiveness.

Section 3.4 Human Resources

Objectives

Some 5,500 personnel were deployed in the operations of the Lehman Administration Companies worldwide at 15 September 2008. The majority of personnel working for the Lehman Administration Companies have employment contracts with LBL, which was the central employing company. Their payroll costs are recharged to the relevant company.

The focus of the team was to:

- Rapidly implement retention processes for critical staff;
- Ensure comprehensive and rigorous processes are implemented for the management of the remaining employees;
- Support the downsizing efforts required to match the skills and resources to the ongoing business needs of the Administration; and
- Manage the operation of the residual HR function.

Progress to date

The position of remaining employees has been stable for some time, following the effectiveness of the early actions in the Administration. Notable areas of progress are:

- Identification of employees who are core to the wind-down and the issuing of contracts for 2009 for c.360 employees;
- The 2008 retention payment process has been concluded. A robust exercise was implemented to ensure that employees were retained and rewarded in an objective performance based process;
- A new operating model was developed to restructure existing teams into workstreams that would support the Administrators. A thorough communication strategy was implemented and re-enforced by the 2009 performance management process;
- A rigorous performance management process for 2009 has been implemented which aligns individual performance and reward to the achievement of specific objectives. Written objectives have been given to retained employees;
- Day-to-day HR support has continued to be provided to employees;
- All HR related issues are being actively progressed including: pension issues, benefit issues and day to day employee issues;
- A comprehensive recruitment process has been implemented to replace any employees who resign during 2009 and/or additional staff needed to optimise the efficiency of the Administration. Some 50 personnel have been recruited to date. Further recruitment is underway, wherever possible through referrals to minimise costs;
- Resolved residual issues relating to the transfer of staff to Nomura;
- All employee claims received in respect of redundancy, holiday pay, arrears of wages and notice payments have been submitted to the Redundancy Payments Office for payment; and
- The process of accumulating all employee residual claims has also commenced.

Key Processes

Two key processes have been introduced to maximise efficiency, control costs and support the achievement of the overall objectives of the Administration:

- **Performance Management**

  All retained employees and all new employees must have documented performance objectives set for 2009.

- **Hiring**

  Where it is identified that additional or replacement resources are required, a rigorous process is undertaken to assess the business justification of the hire and to ensure that the most appropriate and cost effective resource is utilised.

Issues and challenges

Whilst the position of the employees is currently stable there are a number of ongoing challenges in preserving an effective environment for the remaining employees:

- The operating model is fundamentally different to the legacy business and operating framework. This requires continuing support to employees during the transition;

- It is imperative to ensure that employees receive regular communication and details of how their roles form part of the overall operating model;

- The key challenge will be matching human resources to the changing needs of the Administrations going forward, including taking necessary steps to ensure that appropriate resources are in place at all times to ensure that business deliverables are not compromised; and

- Retaining, assessing, rewarding and motivating key employees will be crucial to the overall success of the wind down.

We are confident that the framework implemented will allow these issues to be addressed.

Section 3.5: Pensions

Background

LBL operated one main pension scheme for its employees, namely the Lehman Brothers Pension Scheme (the "Scheme"). The Scheme is administered by its trustees, who have their own professional advisers.

The principal employer of the Scheme is LBL, and in the period before the Administration the vast majority of active Scheme members were employed by LBL. In addition to LBL, the Scheme had a small number of other participating employers, which were not UK entities and did not employ significant numbers of Scheme members.

The Scheme included both defined benefit ("DB") and defined contribution ("DC") sections. Accrual of DB pensions ceased for most members in 1999. As at 31 December 2007 (the year end date preceding the appointment of the Administrators) the Scheme had around 9,500 members, and assets of around £470m, of which some £282m related to the DB category and £188m to the DC category.

Effect of the Administration appointment

The effect of the Administration Order was to start an assessment period for the LBL section of the Scheme under the terms of the Pensions Act 2004, which contains the legislation governing the operation of the Pension Protection Fund ("PPF"). While an assessment period is in place, no further pension benefits are earned and no further contributions are payable, and cover for death in service benefits ceases. In the period after the Administration, we worked with the Scheme trustees to ensure that the effect of the assessment period was communicated to Scheme members.

The start of the Administration, combined with the fact that LBL cannot be rescued as a going concern, also meant that a debt became due from LBL to the Scheme trustees, equivalent to the deficit in the LBL DB section of the Scheme when measured on an annuity buy-out basis. The Administrators have received an initial proof of debt from the Scheme trustees and the PPF for £148m. The Administrators expect to receive a final proof of debt, in which the debt claimed is confirmed in a certificate signed by the Scheme actuary, in due course.

Events after the start of the Administration

The Scheme has given rise to a number of complex issues since the start of the Administration. Most of those issues have been the responsibility of the Scheme trustees, and the Administrators have not needed to be involved. However, where appropriate the Administrators have responded to requests made by the Scheme trustees, including executing deeds in relation to the Scheme on behalf of LBL.

In October 2008 the Administrators received a formal notice from the Pensions Regulator, requiring information concerning LBL and other group companies to be disclosed to the Regulator. The Administrators complied with this notice, and have also maintained dialogue with the Regulator when necessary on other occasions.

There were small amounts (some £50,000) of outstanding pension contributions due to the Scheme as at the Administration date, in relation to certain DC members. Work is underway to seek recovery of those outstanding contributions from the Redundancy Payments Service.

In due course the DB part of the Scheme will either be accepted fully into the PPF or, if it has sufficient assets, wind up outside the PPF. Whilst the outcome for the Scheme is important for the Scheme trustees and members, it is less critical for LBL which is likely to have the same creditor claim from the Scheme in either event. We understand that the trustees intend to wind up the DC part of the Scheme.

Other pension schemes

In addition to the Scheme, LBL had also established a number of small defined contribution pension schemes. LBL itself acted as the trustee of a number of those schemes. An exercise is in progress to wind up the pension schemes concerned.

Section 3.6: Tax

Objectives

The key objectives of the tax function are as follows:

- **Tax Strategy -** to develop an optimal tax strategy for the Administration, taking into account the complexities of the Group;
- **Corporation tax repayments -** to capture, maximise and preserve losses and recover a refund of corporation tax;
- **Management of transactional matters -** management of tax liabilities arising from transactions; and
- **Tax risk management -** to develop procedures to ensure that tax risks are managed.

Progress to date

- We have set processes in place to prepare and control the preparation of corporation tax returns to ensure that compliance obligations are met as necessary;
- We have established essential relationships with HMRC and the Enforcement Office and have conducted meetings to discuss key issues such as:
  - group tax losses and the format and time limits for group relief claims;
  - clarifying the structure of the Group Payment Arrangement (“GPA”) and implications on the GPA and tax recoveries as a consequence of Administration;
  - negotiating with HMRC on on-going enquiries to limit the areas of focus to key issues so that costs for the Administration can be minimised; and
- We have also provided advice on the tax implications of the sale of the Slough Data Centre by ODC3 Limited (of which LBL is a creditor).

VAT

We have reviewed and identified the structure of the Lehman VAT group (of which LBL is the representative member), and established the compliance status, payments position and the status of any ongoing HMRC enquiries.

We have prepared the VAT return for the period from the end of the last pre-appointment VAT period to the date of appointment. This will be submitted shortly.

Key processes

Tax compliance

A robust and efficient process has been developed for the preparation of corporation tax returns. In addition to ensuring that the LBL satisfies its tax compliance requirements, it is necessary for a large number of corporation tax returns to be filed to realise the value of LBL tax losses and obtain a refund of corporation tax.

Issues and challenges

HMRC relationship

Various tax related aspects will potentially be affected or influenced by HMRC (including, in particular, successfully obtaining a refund of corporation tax using Group tax losses).

The tax function has met and spoken regularly with senior inspectors within HMRC to preserve the existing good working relationship and to reach quick agreement on matters that could potentially deplete the value of the estate or delay the tax reclaim process.

Availability of accounting information

In order to file corporation tax returns, accounting records of sufficient quality are required to be maintained. The tax team has worked with other work streams to ensure the necessary information can be made available for the corporation tax compliance process.

Given the extensive demands on the accounting resources within LBL and the limited personnel and access to systems, this has been and remains a challenging objective.

Group Payment Arrangement

Group Payment Arrangements aim to reduce the administrative burden of paying tax liabilities in a large group of companies and operate on an accounting period-by-accounting period basis. The Lehman GPA is a corporation tax payment arrangement between many Lehman UK entities and HMRC. GPAs are not drafted with insolvency in mind. Once party to an agreement, a company must abide by the contract for the whole of the accounting period. LBL is the 'Principal Entity' facilitating the Lehman GPA - prior to our appointment GPAs have been established for all Lehman accounting periods up to and including the 30 November 2008 year end.

As a general rule, corporation tax liabilities (or other UK tax liabilities) of a GPA participating entity may be assessable on any other member of the GPA. To assess whether a corporation tax under or over-payment has arisen all GPA companies must first submit their tax returns for a period. Only then can an application be made to HMRC to recover any tax overpayment.

In summary, the tax issues to address are complex and voluminous – we have implemented a framework to ensure that these are systematically addressed.

Section 3.7 Intercompany

Overview

The global nature of the Lehman business, with highly integrated trading and non-trading relationships across the group led to a complex series of intercompany positions being outstanding at the date of Administration. These include approximately 270 debtor and creditor balances between LBL and the rest of the group representing, by book value, $1.9 billion of receivables and $1.2 billion of payables as at 15 September 2008.

Progress to date

The primary focus at the outset of the Administration was to ensure that the interests of the Lehman Administration Companies were preserved with Lehmans Group companies – in particular meeting the claims filing bar dates set by Lehman Brothers entities in Japan and Switzerland. These claims were filed by the due dates. The intercompany team has continued to make significant progress, including:

- To date claims have been filed against 11 group companies on behalf of all the Lehman Administration Companies, including approximately $16m for LBL;
- Active and regular communication is in place with insolvency office holders across the globe;
- Local representatives have been appointed in key locations - Japan, Hong Kong, Australia and Korea;
- Active dialogue is ongoing with the office holders in Europe, including Switzerland, France, Holland, Luxembourg, Germany and Italy;
- Evidencing standards for both trading and non trading balances have been defined; and
- A secure central repository for storing supporting documentation and evidence for claims has been established.

Key processes

Significant progress has been made as a result of the intercompany team adopting the following approach:

- A team is preparing evidence for intercompany claims;
- A team has been set up to interact with all relevant overseas Insolvency practitioners to progress claims post filing;
- Two specialist teams have been set up to focus on non-trading and exceptional items, supported by an experienced cross disciplined advisory group;
- Creating standardised documentation; and
- Leveraging the organisation to assist in the trading elements of the intercompany validation and claims filing.

Issues and challenges

The intercompany relationships are complex and subject to a multiplicity of legal agreements. They deal with many differing types of activities including financing, swaps, common cash and securities accounts, staff and cost recharges. Although the last two activities are of most obvious relevance to LBL, the resolution of balances relating to the other activities mentioned is also, indirectly, of importance to LBL. The challenges inherent in filing claims across the world for such relationships are many and include:

- A significant volume of securities and non-securities trading transactions;
- Intercompany positions remain subject to market risk where agreements are still live;
- Uncertainties over asset ownership with affiliates and the risk that these entities seek to assert or deny trust claims; and
- Uncertainty over the precise scope and impact of various intercompany guarantees and assignment agreements

Work is ongoing to address these issues.

Section 3.8: Affiliate company relationships

Background

As noted elsewhere in this report, Lehman Group entities and operating systems across the world had a significant degree of interdependency. The various insolvencies across the world, including the appointment of the UK Administrators and the Chapter 11 proceedings in the US, have inevitably resulted in many entities, being unable to access data and resources regarding their financial position, business and operations.

In Europe the material entities with which LBIE, supported by LBL, had a relationship included Lehman Brothers Treasury Co BV (Holland), Lehman Brothers (Luxembourg) SA, Lehman Brothers (Luxembourg) Equity Finance SA, Lehman Brothers Finance SA (Switzerland) and Lehman Brothers Bankhaus AG (Germany).

These and other European affiliates were, to a greater or lesser extent, reliant upon accounting and IT systems maintained primarily by Lehman entities in London. Certain affiliates had their own staff located in London or had access to LBL staff in London. The fact that these various companies have become subject to separate local insolvency processes has proven challenging for both the office-holders managing the separate European affiliates and the Administrators of the Lehman Administration Companies.

LBL employed the majority of Lehman staff based in the UK (and elsewhere in the LBIE branches) and was the contracting party for key infrastructure arrangements (such as IT and property). LBL seconded most of its staff to carry out duties for other group companies. The majority of these were for the benefit of LBIE but certain of these individuals provided day-to-day transactional and technical support to a number of the European entities.

In addition, certain staff arranged and managed transactions for other non-European Lehman entities, including Lehman Brothers Special Financing, Inc. (USA) and Lehman Commercial Paper Inc (USA).

Progress to date

Early in the case it was apparent that both LBL and LBIE's support would be required by various affiliates and bi-lateral discussions were commenced in late September 2008 with a view to collaborating in areas which would mutually benefit the various estates.

US affiliates

The initial concern of the UK Administrators was the relationship with LBHI, the ultimate US holding company. LBL and the other UK affiliates were themselves at least partly dependent upon the US for systems support. This dependency ran both ways, and a Transitional Services Agreement was negotiated by LBL and agreed with LBHI and certain of its affiliates during November 2008.

Since that date considerable support has been provided to LBHI under the TSA on a cost indemnified basis. This has allowed LBHI to further its objectives with LBL and LBIE's support and has ensured that various complex risk and conflict issues are managed. Extensive dealings continue with the team managing LBHI, including daily interactions on issues where LBL or LBIE provides support.

European Affiliates

The UK Administrators, including those managing LBL have offered certain support to various European affiliates. These efforts have included:

- The formation of a dedicated team to manage dealings with affiliates;
- Active dialogue from the inception of the case;
- Meetings in the UK and elsewhere;
- Regular, focussed communication to address specific requests of affiliates;
- Specific proposals for the provision of services and support; and
- Discussion on the manner in which claims will be admitted and proved in the various estates, respecting local requirement of the debtor affiliate.

The provision of services to the affiliates is provided on a cost indemnity basis and can only be provided where there is sufficient, available appropriate human resource or information systems capacity.

As the business models of the individual affiliate companies vary widely the service needs are different. Tailored agreements are being negotiated with affected affiliates.

Other matters

Creditors may be aware that LBHI is currently promoting a far reaching multi-lateral agreement between Lehman legal entities requiring entities to provide rights of access and information to each other. At this time the Administrators do not consider it to be in the best interests of LBL and its creditors to be party to or bound by such a broad arrangement, which could potentially place a very significant burden on LBL, to the cost of its general body of creditors. We will continue to manage LBL's affairs efficiently and effectively, in the interests of its creditors and will continue to provide appropriate levels of professional cooperation with affiliate company office holders dealing with the specific matters which affect LBL's interface with each of them in a tailored manner and LBL's costs of doing so are appropriately recovered.

Section 4: Statutory and other Information

Court details for the Administration:	High Court of Justice, Chancery Division, Companies Court - case 7945 of 2008
Full name:	Lehman Brothers Limited
Trading name:	Lehman Brothers Limited
Registered number:	846922
Registered address:	25 Bank Street, London E14 5LE
Company directors:	D Gibb, CL Heiss, IM Jameson, AJ Rush, PR Sherratt
Company secretary:	M Smith, P Dave, ESE Upton
Shareholdings held by the directors and secretary:	None of the directors own shares in LBL
Date of the Administration appointment:	15 September 2008
Administrators' names and addresses:	AV Lomas, SA Pearson, DY Schwarzmann & MJA Jervis, 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 LBL's creditors as a whole than would be likely if LBL 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 either 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 LBL's net property:	There is no qualifying floating charge holder, so there will be no prescribed part
Whether and why the Administrators intend to apply to court under Section 176A(5) IA86:	Not applicable as there is no prescribed part
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 the proceedings are the main proceedings.

Section 4.1: Statement of Affairs

The Administrators have granted the Directors an extension of time in which to prepare a Statement of Affairs, due to the complexity of the task. Interim submissions have been received from the Directors, which have allowed the Administrators to prioritise and focus their activities on asset recovery and claims management.

The Administrators do not believe it is in the interests of creditors to provide an alternative financial analysis at this time as it could potentially provide a misleading view of the recovery prospects for creditors. To the extent that this report has included extracts from the information provided, such extracts are not comprehensive and no reliance should be placed upon them in forming any view of the dividend prospects for unsecured creditors.

Whilst the directors have provided details on the value and identity of creditors at 15 September 2008, according to the books and records at that date, actual claims by creditors will differ materially.

As covered previously in this report, LBL is a shareholder of Lehman Brothers International (Europe) – in Administration, an unlimited company and is therefore liable for any shortfall to creditors of that estate. This would further increase the eventual level of claims in LBL.

Section 5: Joint Administrators’ Remuneration

Background

This section sets out the process for setting and monitoring the Administrators’ remuneration.

In this case, the Committee is responsible for agreeing the basis and quantum of the Administrators’ remuneration.

Insolvency Rules 1986

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

There are two alternative bases under the Insolvency Rules 1986, 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 Insolvency 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 to 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 (“SIP9”)

In addition to the Insolvency Rules, SIP9 provides guidance to insolvency practitioners and creditors’ committees in relation to the remuneration of, *inter alia*, Administrators. The purpose of SIP9 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 fees 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.

The Committee members have each been provided with a copy of SIP9.

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 SIP9 the Committee has been provided with details of the charge-out rates of all grades of staff which are involved on the case.

As the remuneration is based on time costs the Committee has been provided with the time spent and the charge-out value, together with additional information setting out the approach to the project.

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

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

In both cases the level of analysis and disclosure to the Committee has met or exceeded these standards.

SIP9 also suggest 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 fee agreement;

- Any existing agreement about fees; 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 length in the sessions we have held with your Committee.

Members of the Committee are bound by a confidentiality undertaking as some of the matters we have covered with them are commercially sensitive and could impact the level of recoveries by creditors if disclosed.

Resolutions of the Creditors' Committee

To pay costs on a "time properly given" basis

Given the fundamental uncertainties about the value of the property with which the Administrators have to deal with the Committee resolved to use the "time properly given" basis –i.e. an hourly billing basis.

Fee rates

Details of the hourly fee rates have been provided to the committee, together with any available market benchmarks.

Cost approvals to date

To date the Committee has approved remuneration of £1,178,138 which comprises 2,986 hours at an average hourly rate of £394.55.

The table below provides an analysis of the total hours and cost by grade of staff:

Global Grade	Total Hours	Total £
Partner	204	163,049
Director	272	179,494
Senior Manager	589	304,009
Manager	575	209,445
Senior Associate	717	201,025
Associate	629	121,116
Grand Total	**2,986**	**1,178,138**

The Committee has also resolved that the Administrators may draw 75% of their time costs on account to assist with the smoothing of working capital. All such costs are subject to detailed reporting to the Committee and ultimately subject to their approval. We have drawn an additional £171,752, which represents 75% of our outstanding time costs for February 2009.

It is likely that current levels of activity will be sustained for some time and we therefore expect that these costs will continue to accrue at a similar rate over the coming months.

Section 6: Receipts and Payments to 14 March 2009

	GBP	EUR	USD	As at 14 Mar 09 Total (USD Equivalent)
	mil	mil	mil	mil
Receipts				
Payroll recharge receipts	138.5	-	36.6	230.0
Building recharge receipts	49.4	-	-	69.0
Loan from LBIE	17.8	2.6	14.2	42.4
Receipts from third party purchaser and LBHI	24.8	-	-	34.6
Other	4.9	0.3	4.0	11.5
VAT received	0.9	-	-	1.2
Total receipts for period	**236.3**	**2.9**	**54.8**	**388.7**
Payments				
Payroll and employee costs	(155.6)	(2.5)	(12.8)	(233.5)
Building and occupancy cost	(38.4)	(0.1)	(3.5)	(57.3)
Payments to LBIE in respect of loan and other items	(23.8)	-	(34.1)	(67.3)
Legal fees	(2.2)	-	-	(3.1)
Payments for group companies	(1.7)	-	-	(2.3)
Administrators' remuneration	(1.3)	-	-	(1.9)
Other advisors' costs	(0.4)	-	-	(0.6)
Other cost	(2.6)	-	-	(3.6)
VAT paid	(3.4)	-	(0.4)	(5.1)
Total payments for period	**(229.4)**	**(2.6)**	**(50.8)**	**(374.7)**
Net position	**6.9**	**0.3**	**4.0**	**14.0**
Bank balances				
Bank of England	2.4	0.3	1.5	5.1
HSBC	4.5	-	2.4	8.8
Barclays	0.0	0.0	0.1	0.1
Balance	**6.9**	**0.3**	**4.0**	**14.0**