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# *Lehman Brothers Limited – In Administration*

## Joint Administrators' progress report for the period 15 March 2010 to 14 September 2010

12 October 2010

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# Contents

# Section 1 Purpose of the Joint Administrators' progress report

## Introduction

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

This is the fourth such report and provides an update on the work that the Administrators have undertaken, with particular focus on the progress made during the six months since 15 March 2010.

## Objectives of the Administration

The 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

The Administrators regularly meet with the Creditors' Committee (the "Committee") and, to date, ten 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 the Committee on critical issues.

## Outcome for unsecured creditors

The 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 ("LBIE"), an unlimited company. LBL is therefore potentially liable for any shortfall to creditors of that estate. Clearly, this could have a significant impact on funds available to other 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 Joint Administrators' actions to date

LBL was pivotal to the operations of the Lehman Brothers Group of companies (the "Group"), as it held most of the UK Groups' service contracts and employee contracts. LBL also maintained IT and general infrastructure to support the needs of the Group. It is also the head lessee of the former European headquarters at 25 Bank Street, Canary Wharf.

In Administration, LBL has continued to provide services to other UK-based Lehman Brothers Companies in Administration (the "Lehman Administration Companies") and to receive cash from other Group entities to cover these costs. LBL has been able to reduce the number, and value, of creditor claims it will receive.

Since their appointment, the Administrators have used specialist teams from within PricewaterhouseCoopers LLP ("PwC"), working with retained LBL employees, to ensure that the operations of LBL are properly coordinated and the objective of the Administration is met. The teams are formed around the following activities:

- Infrastructure and property;
- Information technology;
- Human resources;
- Pensions;
- Corporation Tax and VAT;
- Intercompany;
- Affiliate company relationships; and
- Recharges.

We comment in more detail on the activities of the teams in the following pages of this report.

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 their progress and ensuring that they have appropriate resources.

Key progress since 15 March 2010 includes:

- Continued retention of the core employee group and completion of 95 new hires in the Report period with performance management and incentive arrangements agreed to support the retention of employees;
- The continued implementation of the Information Technology ("IT") change program to rationalise the technology footprint and reduce costs;
- The successful execution of complex IT projects, enabling separation from Barclays Capital and Nomura;
- The establishment of a mechanism for securing tax repayments in the Group is now in the final stages of being agreed with all stakeholders. To date LBL has received £62m in tax repayments on behalf of the Group Companies; and
- Substantial progress in defining arrangements for ceasing to manage 25 Bank Street.

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 these assets for the benefit of the creditors of LBL, and minimising of obligations to creditors.

# 2.1 Infrastructure and Property

### Overview

The role of Infrastructure and Property ("I&P") is to manage the premises of 25 Canada Square to support the Lehman Administration Companies and continue to manage the premises of 25 Bank Street for the subtenants. The majority of the costs incurred for the continued management of 25 Bank Street are recovered by LBL from the various subtenants.

The focus of the I&P team has been to:

- Reduce LBL's cost base through relocating the Lehman Administration Companies to premises leased by another Group entity at 25 Canada Square, Canary Wharf;
- Continue to manage 25 Bank Street for the subtenants;
- Continue essential IT and property services;
- Coordinate the recovery of costs incurred from subtenants; and
- Realise value for creditors from physical assets.

### Progress

The key highlights for the period were:

- The smooth transition of the Lehman Administration Companies to 25 Canada Square, effective 31 March and significantly reducing costs;
- From 31 March, minimising landlord services at 25 Bank Street, reducing management costs to a minimum;
- Preparation for the removal of all ties from 25 Bank Street including disconnecting all IT infrastructure and the termination of all supplier obligations relating to 25 Bank Street with effect from the termination of subleases to Nomura on 30 September 2010;
- Discussions with Canary Wharf Group regarding the future of the head lease of 25 Bank Street;
- Initiated future data centre provisioning discussions with Global Switch; and
- The continued negotiation of IT contracts for software and applications on commercial terms with existing and new vendors.

The I&P team continued to successfully manage essential services for the ongoing operation of the Lehman Administration Companies at 25 Canada Square in addition to:

- Managing the reduced services for subtenants at 25 Bank Street; and
- Preparing for the auction of the art collection (substantially completed in late September 2010, after the end of the report period).

### Issues and challenges

The main challenge encountered by the I&P team has been in managing the transition of the Lehman Administration Companies to 25 Canada Square, including the reduction of service levels at 25 Bank Street and the termination of all related supplier obligations.

The second significant challenge has been the negotiation of IT software and application licenses. This has been resolved through the relationships established with vendors during the Administration.

In the next six months, the key challenges are:

- Surrender of the head lease of 25 Bank Street; and
- Completion of negotiations with Global Switch for the future provision of data centre facilities.

## 2.2 Information Technology

### Overview

The role of the IT team is to provide a secure, stable, cost effective and appropriate technology platform to facilitate the activities and financial objectives of the Lehman Administration Companies, most notably to LBIE.

The key tasks required to deliver the short term objective of maintaining the operational technology platform include:

- Support of applications required by the business, including the central systems developed specifically to support the core Administration activities and processes;
- Delivering robust IT security;
- Managing the service delivery from Nomura and Barclays Capital;
- Managing contracts with key external parties; and
- Supporting forensic investigations.

The long term objective to achieve independence and rationalise the technology footprint is being delivered through the following core interdependent initiatives:

- Forensic data capture;
- Application rationalisation and migration; and
- IT infrastructure rationalisation.

### Progress

Specific progress in this period includes:

- Dependency on Nomura for provision of IT services has been removed except for some low levels of support of legacy infrastructure;
- Dependency on Barclays Capital IT infrastructure and applications has been removed;
- The majority of applications have either been retired or migrated into the Administration's independent data centre. The remaining applications will be migrated during the next period; and
- The strategic systems that are central to the Administration have been further developed to support the Trust Claims Resolution Agreement (for LBIE) and unsecured creditor initiatives.

### Independence

- 13 million critical reports and documents held on Barclays Capital and Nomura systems have been transferred to the independent data centre;
- Alternative systems have been implemented to substitute the application functionality provided by Barclays Capital;
- Forensic data identified as critical to support investigations and litigations has been captured and stored;
- Business applications have been either retired or migrated into the independent data centre;
- The network that has been shared with Nomura since the sale of the business was separated in September; and
- Knowledge transfer of data centre and infrastructure operations from Nomura is almost complete.

### Central systems

- The systems architecture that is strategically important to the core operations of the Administration has been reviewed and aligned to the Administration's broader strategy;
- The asset tracking system that generates a single counterparty view has been enhanced to include unsecured creditor functionality and client settlement reporting; and
- The client portal that is used as the primary interface to counterparties has been further developed to incorporate the requirements to support unsecured creditors.

### IT Infrastructure

- The two legacy data centres have been rationalised to a single data centre in readiness for independence from Nomura's support in October;

- IT dependency on 25 Bank Street has been successfully removed; and
- Rationalisation of the IT infrastructure and migration to a smaller space continues with planned completion in the next period.

The process to outsource the operations of the data centre and infrastructure is underway with planned implementation in the next period.

### *Issues and challenges*

- Although there has been substantial simplification since the start of the administration, the IT environment remains complex. In order to successfully outsource the operations as planned significant effort is required to rationalise and remove some of the complexity; and
- The requirements from the business on IT continue to evolve rapidly and IT needs to remain flexible and responsive during a period of significant infrastructure change.

Throughout the next six months IT will focus its efforts on the following initiatives whilst maintaining the priority of providing a stable and secure environment for the Administration:

- Transfer management and control of IT from LBL to LBIE;
- Reduce the cost and complexity of running IT;
- Align the systems architecture with the business critical objectives; and
- Develop long term data management strategy.

# 2.3 Human Resources

## *Overview*

Human Resources ("HR") is responsible for all matters relating to the retention, resourcing, reward and restructuring of LBL's employees.

The majority of employees working for the Lehman Administration Companies have employment contracts with LBL, and their payroll costs are recharged by LBL accordingly.

The retention and management of staff is critical to achieving the objectives of the Lehman Administrations in the most efficient and effective manner.

The focus of the HR team has been to:

- Provide day-to-day support for employees, fixed term contractors and consultants, including the handling of HR issues for the Administration relating to:-
  - Reward;
  - Pensions;
  - Benefits;
  - Employee claims;
  - Statutory employee requirements; and
  - Mitigation of employee risk.
- Drive the Performance Management Process;
- Complete all required monthly tax reporting relating to employees;
- Manage day to day employee issues in a "business as usual" environment;
- Develop and implement a leadership and development programme for all employees;
- Support the future resource planning, and retention strategies; and
- Ensure appropriate cost recharging of employee costs.

The Administrators expect to retain a significant proportion of the Lehman employees for an on-going period.

## *Progress*

The overall employee population has continued to be relatively stable in this period, with a manageable level of turnover and focussed replacement hiring.

Notable areas of progress in the period are:

- Targeted recruitment of 95 new people. A focus on direct and low fee hiring generated a saving in recruitment costs of c.£500k;
- Management of the mid-year performance review process. Employees were reviewed against individual objectives as well as the newly introduced key competencies and key standard objectives for all Managing Directors and Executive Directors (completed with 100% compliance);
- Determining the anticipated resource profile for 2011;
- Development of the 2011 Retention Strategy with the implementation of the 2011 Retention Unit Award Program which rewards employees who remain committed to achieving the overall objectives of the Administrations;
- Continued progress with Her Majesty's Revenue and Customs ("HMRC") to resolve pre and post-Administration PAYE reconciliation;
- Preparation of all year-end reporting requirements to HMRC including P35 and P11Ds;
- Ongoing activity regarding employee related debt recovery; and
- Continued development of the Leadership and Development programme to support performance and retention of employees.

## *Issues and challenges*

The employee dynamic has evolved as the Administrations progress. A number of challenges are being addressed to ensure appropriate resources are in place to support the achievement of the overall objectives including:

- Review of employee skill base against resource requirements of the Administration;
- Encouraging redeployment and sharing of resources to meet specific objectives; and
- Retaining, assessing, rewarding, and motivating key employees to support the Administrations.

Over the next 6 months, the HR Team will focus on the following areas:

- Reviewing the 2011 resource requirements and implementing appropriate recruitment, retention and cost control processes to meet these requirements;
- Operating a robust year end performance management process to ensure employees are rewarded based on their performance against objectives and key competencies;
- Managing the 2011 objective setting process to ensure employee objectives are aligned to Team and Administration objectives;
- Ongoing management of employee issues, mitigating employee relation risks and supporting any further employee transfers to new companies;
- Resolving issues relating to the offshore Employee Benefits Trust; and
- Agreeing employee claims & mitigating where possible.

# 2.4 Pensions

## *Overview*

LBL operated one main pension scheme for its employees, namely the Lehman Brothers Pension Scheme (the "Scheme"). LBL is the principal employer of the Scheme, which included both defined benefit and defined contribution sections (although in practice it is only the defined benefit section which is now relevant in the Administration). The Scheme continues to be administered by its Trustees.

The main areas of activity have been to liaise with the Scheme (represented by its Trustees and the Pension Protection Fund ("PPF")) in relation to its role as a creditor of LBL in respect of the defined benefit section of the Scheme, which is in an assessment period for the purposes of the PPF, and to respond to requests for information from the Pensions Regulator.

## *Progress*

Shortly after the start of the Administration, the Administrators received an initial statement of claim from the Scheme trustees and the PPF for £148m. The Administrators have been informed by the Scheme trustees that a final statement of claim should be ready for submission by the end of 2010.

The Administrators have received a number of additional formal notices from the Pensions Regulator, requiring disclosure of various items of information concerning the Lehman Brothers Group in the UK. The Administrators have responded to these notices as appropriate.

The Administrators are aware that a Determination Notice has been issued by the Pensions Regulator, stating that a Financial Support Direction ("FSD") will be issued against six Lehman entities (including four of the Lehman Administration Companies, but excluding LBL), subject to the right of those entities to refer the Determination to the Upper Tribunal (Tax and Chancery) for a re-hearing. The Administrators are keeping under review the implications of this FSD process for LBL.

# 2.5 Corporation Tax and VAT

## *Overview*

The tax structure is complex and the issues for LBL are closely connected with those of the Group. Securing tax repayments for the Group of up to £430m is the key aim, but protecting tax losses for the future is also essential, as tax arising post-Administration is an expense of the Administration.

The key objectives for the Tax team are as follows:

- **Corporation tax repayments** – to bring the tax affairs of the Group up to date and facilitate the recovery of tax paid in prior years. The work has developed into careful planning of loss utilisation to minimise post-Administration tax liabilities;
- **Tax strategy** – maintaining the tax Group to maximise Group tax planning opportunities in the post-Administration periods;
- **Transaction tax planning** – managing tax liabilities arising from transactions, to maximise the return to the estate; and
- **Tax risk management** – developing procedures to ensure that tax risks are managed within LBL and the Group, to avoid tax leakage.

## *Progress*

Specific progress in the period includes:

### Corporation Tax

- All accounts and tax computations are required for companies within the Group, LBL being the representative member co-ordinating the Group tax relationship with HMRC. Significant progress has been made to bring outstanding accounts and tax computations up to date. All computations for 2007 have been submitted and only six computations for 2008 remain outstanding. 32% of the computations for the 2009 year end have been submitted;
- The mechanism through which tax and tax losses are equitably allocated across the Group for years 2004-2007 is in the final stages of being agreed with all stakeholders. The final 2004-2007 Group tax position will be submitted to HMRC in early October. The benefit from this submission is an anticipated increase in tax repayments being made to the Group from HMRC; and
- The timing of the tax recovery is uncertain, given the current economic climate. To date tax repayments of £62m have been made to the Group.

### VAT

- The May 2010 VAT return is undergoing final review for submission to HMRC;
- As at 14 September 2010 HMRC had repaid the February, May and August 2009 VAT Group returns. A further £5.4m repayment, relating to the November 2009 VAT Group return was subsequently received, resulting in a net repayment of £24.2m. Individually, however, LBL is in a net payment position;
- Information is being collated for the August 2010 VAT return for submission to HMRC which will bring the VAT return position up to date; and
- HMRC have agreed to settle the Fleming claims submitted relating to the pre-appointment period amounting to £1.5 million plus statutory interest of £2.2 million.

## *Issues and challenges*

- **Accounting** – The preparation and submission of tax computations depends upon draft accounts being prepared for open years. Given the complex accounting and specialist resources required, preparing the appropriate accounts is not straight forward. The target is for all of the 2009 tax computations to be submitted within the next few months; and
- **Tax repayments** – Through ongoing correspondence with HMRC a £62m Group tax repayment has been received to date. The submission of the 2004-2007 Group tax position in October should result in additional tax repayments later this year.

A complexity to the repayment of corporation tax is the application of set-off, where repayments due to some Group companies may be set-off against tax liabilities of other Group companies.  HMRC's enforcement office have yet to opine on this matter, which has been outstanding since November 2008.

Over the next six months the Tax team will focus on the following areas:

- Submission of the remaining 2008 and 2009 tax computations and Group tax loss schedules to ensure tax filings are up to date, thus facilitating the recovery of tax paid in prior years;
- Continued liaison with HMRC to ensure timely repayment of tax; and
- Group tax planning to minimise tax leakage in post administration periods.

# 2.6 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 289 debtor and creditor balances between LBL and the rest of the Group representing, at book value, $1.8bn of receivables and $1.3bn of payables as at 15 September 2008. These amounts have changed since the last progress report and are discussed later in this section.

The primary focus at the outset of the Administration was to ensure that the interests of the Lehman Administration Companies were preserved, in particular meeting the claims filing bar dates set by other Lehman Brothers entities. This remains a key focus but there have been no new bar dates announced for which LBL has needed to make a claim in the last 6 months.

Instead, the primary focus has shifted towards progressing the balances with Affiliates with a view to maximising the monies recovered.

## *Progress*

The Intercompany team has continued to make significant progress in these and other areas, including:

- Active dialogue with the office holders in the US, Asia and Europe, including UK, Netherlands, Germany, Luxembourg, Switzerland. The focus of this effort has been the largest balances as well as those where the Affiliate concerned is not in an insolvency process. Progress is monitored by regular reports showing the status of the largest 100+ Affiliate balances and the methods being used to maximise recoveries (i.e. enforcement letters and legal recourse being considered or employed).
- Significant time has been spent in the last 6 months working with Alvarez and Marsal in the US and UK on the following items:
  - The LBHI Plan of Reorganisation which deals with the direct and guarantee claims of LBL against LBHI and the other Chapter 11 Affiliates. Whilst not complete, a good working draft has been produced and residual issues are being worked through; and
  - The LBL claim against Lehman Brothers Luxembourg Investments SARL (LBLIS). Again, whilst not yet agreed by the Directors of LBLIS, forensic evidencing has enabled strong factual proof to be presented and has resulted in increased confidence that the claim (LBL's third largest) will ultimately be successful.
- Proactive evidencing packs for agreeing general Affiliate balances have now concluded and the centralised independent evidencing team has largely been disbanded. The evidence prepared has been stored in a secure central repository. Ad hoc requests for evidence by the office holders for Affiliates are still being responded to by the residual staff; and
- The team responsible for claims progression has migrated their records away from e-mail and proprietary spreadsheets to a strategic Client Relationship Management platform used throughout the Lehman Administration Companies.

## *Issues and challenges*

Affiliate relationships are complex given the multiplicity of locations and arrangements between Affiliates. LBL provided multiple services to Affiliates under various legal agreements including staff, premises and other expense recharges. LBL has also provided services to Affiliates in circumstances where a formal agreement had not been entered into, this lack of formality creating additional requirements for clarifications when seeking to recover monies due.

The recovery of LBL intercompany debts is contingent on the recovery of assets in LBL's Affiliate debtors and whilst LBL's primary focus has shifted towards progression of the balances with Affiliates, this interrelationship has restricted recoveries in the period to $200k. Overall however, the LBL Affiliate claims process remains well advanced when compared to other office holders globally.

Some of the challenges around progression of the Affiliate balances are specific to LBL. The book value of Affiliate receivables and payables has been restated, as it has been determined that agreeing a starting point for Affiliate balances will be easier if some of the material items around which estimates have been made, namely staff pensions and service invoices are removed. This only impacts a relatively small number of Affiliate balances, but has the impact of changing the gross receivables and payables.

The remainder of 2010 and the first few months of 2011 is likely to see continuing focus on agreeing claims already made and progressing receivables from Group companies not in an insolvency process.

# 2.7 Affiliate company relationships

## *Overview*

LBL continues to provide appropriate levels of professional cooperation with Affiliate Company Office Holders, dealing with these relationships on an individual bases, governed through appropriate bilateral agreements between the parties. Such agreements will ensure that LBL's costs of supporting such Affiliates are appropriately recovered.

Due to the nature of LBL as a service company, employing the majority of Lehman staff in the UK, as well as maintaining the IT infrastructure and property arrangements, LBL's support to other Lehman entities continues to be an ongoing requirement. LBL has sought to ensure that the support required by various external Affiliates has been managed in a manner that demonstrates clear benefits to LBL's creditors in its provision.

## *Progress*

LBL has continued to provide assistance to LBHI and its Affiliates' under the LBHI Transitional Service Agreement ("TSA").

In the six month period to 14 September 2010 a further three bilateral agreements, to provide scoping services and data, have been signed, bringing the total to nine.

To continue to service the large number of requests for specific data, LBL has maintained an Affiliate data request team. This team, working closely with Data Governance, IT and the Affiliate team, administer the complex technical requirements in extracting and separating large quantities of data. The team operates under the bi-lateral agreements and recovers its costs, together with an uplift and a contribution towards application costs, under these same agreements.

### LBHI

Considerable support has been provided under the TSA with LBHI since it was signed in November 2008. The amount invoiced to the LBHI Estate (including Neuberger Berman), to 14 September 2010, totalled £62.1m. This includes salary re-charges and significant continuing monthly charges for IT access and data provision. In comparison, in the same period, LBHI has invoiced to LBL a total of £13.8m, predominantly for staff recharges.

In accordance with the aims of the TSA, reducing the level of interdependence between LBL and LBHI remains a priority. By September 2010 shared personnel resources were reduced to only four people. Whilst there remains a continuing level of IT support, LBL's ongoing IT decommissioning process and the continued streamlining of IT assistance has meant a reduction of 20% in the total number of applications used by LBHI.

The TSA signed with LBHI is scheduled to end on 13 November 2010. Although interdependence has greatly reduced over the past 24 months, a level of co-operation from both sides would be desirable to continue an efficient and timely winding down of the respective estates. To that end early talks have started with a view to negotiating a framework for further co-operation.

### Other Affiliates

The Administrators have continued to offer support to various other (non-LBHI) Affiliates including updates on the transformation of the Lehman Administration Companies' environment and the implications this has for Affiliates requiring data.

A total of eight agreements have now been signed with Affiliates other than LBHI. This includes three concluded in the last six months with Lehman Brothers Finance, Lehman Brothers Bankhaus and Lehman Brothers Inc. Substantial progress has been made in the period with each Affiliate.

It is not expected that any further data agreements will be concluded, as the deadline for these has now passed. However, requests under the existing agreements are likely to take several months further to process.

The amount invoiced to non LBHI Affiliates up to 14 September totals £1.3m, which is predominantly time-costs, but also includes a £0.4m contribution to application costs.

## *Issues and challenges*

The provision of services to the Affiliates can only occur where there is sufficient, available and appropriate, human resource and IT capacity. IT decommissioning has already reduced LBL's ability to service certain Affiliate requests and this is likely to continue.

Risk management remains a vital aspect of Affiliate company relations, not just in terms of data provision and the risks surrounding co-mingled data, but in terms of investing in relationships. Each Affiliates' business model varies widely and all agreements are tailored to address the different conflicting requirements.

# 2.8 Recharges

## *Overview*

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 do not necessarily benefit LBL on a standalone basis.

The priority upon appointment was to establish and implement a cost recharge agreement to provide 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 have apportioned the total budgeted costs across the Group companies, based on the proportion of Lehman Group staff working in 25 Bank Street or 25 Canada Square on behalf of each company. This method was decided upon as it gives an indication of the level of activity being carried out in each company and the costs incurred in support of that activity.

## *Progress*

Despite the move from 25 Bank Street into 25 Canada Square in March 2010, the cost recharge mechanism continues to be used as the mechanism under which LBL pays suppliers and recharges Group entities for costs incurred.

LBIE accounts for approximately 97% of Lehman Group staff working at 25 Canada Square and as a result LBIE is responsible for that percentage of building, occupancy and operational costs, to the extent these are incurred by LBL. In recognition of this, regular meetings are held with LBIE to discuss the costs incurred and the amount to be recharged.

As at 14 September 2010 invoices totalling over £383 million had been issued to the Lehman Group companies under the cost recharge agreement.

## *Issues and challenges*

The recharge mechanism remains complex, although simpler now than at the start of the administration. We continue to exercise vigilant control over amounts owed to LBL and have implemented new procedures to reduce our exposure, such as requiring payroll recharges to be paid before the payroll date. We will continue to monitor these positions closely.

We have completed a reconciliation of all recharges and costs incurred during the course of the administration and are close to agreeing a closure statement with LBIE, so that a new mechanism can be implemented on a bilateral basis between LBIE and LBL.

# Section 3 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:* | Level 23, 25 Canada Square, London E14 5LQ, United Kingdom |
| *Company directors:* | D Gibb (resigned 17/07/2009), CL Heiss (resigned 31/10/2008), IM Jameson (resigned 17/07/2009), AJ Rush (resigned 28/10/2008), PR Sherratt (resigned 06/10/2008) |
| *Company secretary:* | M Smith, P Dave, ESE Upton (all resigned 25/01/2010) |
| *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 and DA Howell, 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. |
| *Details of any extensions of the initial period of appointment:* | The Court has granted an extension of the Administration to 30 November 2011. |
| *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 Joint Administrators' Remuneration

## Background

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

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

## Insolvency Rules 1986

By way of context, the manner in which the 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

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; and
- 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; and
- Assistants and support staff.

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

SIP9 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 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.

## *Resolution 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, the Committee resolved to use the "time properly given" basis – i.e. an hourly billing basis.

### Hourly rates

In accordance with SIP9, details of the hourly rates have been provided to the Committee.

### Cost approvals to date

For the period 15 March 2010 to 14 September 2010, the Committee has approved remuneration of £2,926,642 which comprises 12,216 hours at an average hourly rate of £239.57.

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

| Global Grade | Total hours | Total (£) |
|---|---|---|
| Partner | 82 | 76,986 |
| Director | 234 | 199,827 |
| Senior Manager | 1,763 | 726,215 |
| Manager | 979 | 327,171 |
| Senior Associate | 5,407 | 1,048,744 |
| Associate | 3,751 | 547,699 |
| Grand Total | 12,216 | 2,926,642 |

Remuneration approved by Committee includes £1,830,413 for work performed for and recoverable from Affiliate companies.

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. In the six-month period from 15 March 2010 to 14 September 2010 we drew remuneration of £1,406,314, which (together with amounts drawn in previous reporting periods) represents 100% of our time costs to 14 May 2010 as approved by the Committee, and 75% on account of our time costs from 15 May 2010 to 31 May 2010.

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 5 Receipts and Payments to 14 September 2010

| | GBP (mn) | EUR (mn) | USD (mn) | Other (GBP Equiv) (mn) | As at 14 Sept 2010 Total in GBP (mn) | As at 14 Mar 2010 Total in GBP (mn) | Movement GBP (mn) |
|---|---|---|---|---|---|---|---|
| Receipts | | | | | | | |
| Contribution from third parties* | 116.9 | 0.5 | 11.9 | – | 125.1 | 105.0 | 20.1 |
| Building recharge receipts | 121.0 | – | – | – | 121.0 | 121.0 | – |
| Payroll recharge receipts | 281.9 | 0.1 | 45.4 | – | 311.5 | 280.1 | 31.4 |
| Loan from LBIE | - | – | – | – | – | – | – |
| Other (including realisations) | 22.6 | 2.2 | 4.6 | 0.1 | 27.5 | 26.4 | 1.1 |
| HMRC receipts | 80.6 | – | – | – | 80.6 | – | 80.6 |
| VAT received on invoices | 7.9 | – | – | – | 7.9 | 6.7 | 1.2 |
| Total receipts for period | 630.9 | 2.8 | 61.9 | 0.1 | 673.6 | 539.2 | 134.4 |
| Payments | | | | | | | |
| Building and occupancy cost | (151.4) | (0.3) | (62.8) | – | (192.5) | (161.2) | (31.3) |
| Payroll and employee costs | (295.9) | (2.7) | (34.4) | – | (320.7) | (293.5) | (27.2) |
| Other costs | (2.3) | (0.2) | (0.1) | – | (2.6) | (3.0) | 0.4 |
| Payments to LBIE in respect of loan and other items | – | – | – | – | – | – | – |
| Other advisors' costs | (1.3) | – | – | – | (1.3) | (1.1) | (0.2) |
| Legal fees | (7.2) | – | – | – | (7.2) | (6.4) | (0.8) |
| Administrators' fees | (5.6) | – | – | – | (5.6) | (4.3) | (1.3) |
| VAT payments as group representative | (13.1) | – | – | – | (13.1) | – | (13.1) |
| VAT paid on invoices | (13.6) | – | (1.4) | – | (14.3) | (11.0) | (3.3) |
| Intercompany transfer | (1.5) | – | – | – | (1.5) | (1.4) | (0.1) |
| Total payments for period | (491.9) | (3.2) | (98.7) | – | (558.8) | (481.9) | (76.9) |
| Inter-currency transfers | (24.9) | 2.7 | 37.4 | – | 1.7 | 2.3 | (0.6) |
| Net position | 114.1 | 2.3 | 0.6 | 0.1 | 116.5 | 59.6 | 56.9 |
| Bank balances | | | | | | | |
| Bank of England | 1.0 | 0.2 | 0.1 | – | 1.2 | 1.2 | – |
| HSBC | 113.1 | 2.1 | 0.5 | 0.1 | 115.3 | 58.4 | 56.9 |
| Balance | 114.1 | 2.3 | 0.6 | 0.1 | 116.5 | 59.6 | 56.9 |

*Includes elements of building & occupancy and payroll related recharges
GBP £ equivalent is for information purposes only.
Rates used for conversion are Financial Times rates on 14 September 2010 and 14 March 2010 respectively.
1 USD $ = 0.6492 GBP £
1 EUR € = 0.8333 GBP £
1 USD $ = 0.6598 GBP £
1 EUR € = 0.9088 GBP £