
Lehman Brothers Limited – In Administration

Joint Administrators' progress
report for the period 15 March 2012
to 14 September 2012

10 October 2012

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Section 1 Purpose of the Joint Administrators' progress report

Introduction

This progress 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 eighth such progress 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 2012.

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, fourteen meetings of the Committee have taken place.

The meetings with the Committee provide the Administrators with the opportunity to explain in detail how the Administrators 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. Ongoing legal advice is being obtained and updated on this.

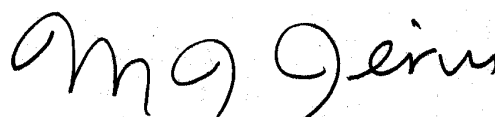
Extension of the Administration

As previously reported, on the application of the Administrators, the High Court granted an Order on 2 November 2011 to further extend the period of the Administration to 30 November 2013.

Future reports

The Joint Administrators' next progress report to creditors will be sent in approximately six months.

Signed:



MJA Jervis
Joint Administrator
Lehman Brothers Limited

Section 2 Joint Administrators' actions to date

As previously reported, 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 was also the head lessee of the former European headquarters at 25 Bank Street, Canary Wharf.

LBL has continued to provide services whilst in Administration to other UK based Lehman Brothers Companies in Administration (the 'Lehman Administration Companies') and has received cash to cover the associated costs of providing such services. LBL has been successful in reducing the number and value of creditor claims it will receive and over time LBL is continuing to reduce the level of services it provides by either discontinuing specific services or passing service provision to end users.

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 currently formed around the following activities:

- Human Resources & Pensions;
- Corporation Tax and VAT;
- Intercompany;
- Affiliate company relationships; and
- Recharges.

The Administrators comment in more detail on the activities of the current teams in the following pages of this progress report.

As previously reported, LBL's assets primarily comprised fixtures, fittings, IT assets, tax refunds and 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.

Key progress since 15 March 2012 includes:

- Further recoveries of corporation tax and VAT repayments on behalf of Group companies. During the period covered by this report, LBL has received corporation tax & VAT repayments of £20.7m on behalf of itself and other Group companies;
- A sustained steady workforce and continued progression in the collection of outstanding employee-related loan and tax amounts, with £1.99m being received in the period;
- As explained in our last progress report, costs incurred by LBL which are recharged to other Group companies under a cost recharge agreement are now limited to payroll and a small amount of ancillary costs. In the six months to 14 September 2012, total receipts under that recharge agreement amounted to £24.8m. Total receipts under the cost recharge agreement, including an element of third party receipts, now stands at £689.8m;
- Agreement of more than 50% of the possible former employee preferential claims. It is anticipated that payment of agreed preferential claims will commence within the next six months; and
- The receipts and payments account on page 10 shows cash held in the six month period reducing by £53.3m. This is primarily a result of corporation tax refunds received for other Group companies being paid over. In the period, cash held for LBL's own account has increased by £22.1m.

2.1 Human Resources and Pensions

Overview

Human Resources (“HR”) is responsible for all matters relating to the provision of ongoing ‘business as usual’ HR support to c.500 LBL employees and contractors. The cost effective management of a stable workforce continues to be critical to achieving the objectives of the Lehman entities in Administration.

Highlights

We have retained a stable and flexible workforce to meet resourcing requirements. 60% of the workforce are engaged on on-going contracts, 25% are on Fixed Term Contracts and 15% are contractors.

Significant progress has been made in resolving former employees’ preferential and non-preferential unsecured claims.

Progress

Notable areas of progress include:

- Completed the 2012 mid-year performance management process, with 100% compliance and individual performance assessed against objectives set;
- Developed the strategy for managing redundancy processes in 2013 and beyond;
- Finalised the 2013 reward package; first grant under the 2013 Retention Unit Awards to eligible employees meeting performance levels;
- Formal review of the Fixed Term Contract employees with extensions to contracts into 2013 offered to 103 employees;
- Continuation of employee development with 16 employees transferring to new roles in this period and 44% of employees attending formal Leadership & Development opportunities;
- Employee benefit renewals completed;
- Significant progress with HMRC to resolve pre and post-Administration PAYE / NIC reconciliations;

- Preparation and distribution of P11D information and finalisation of tax year end P60 and P35 reporting;
- Continued progress made in the recovery of outstanding loans due to LBL from former employees, either directly or in connection with expatriate tax loans, with £1.99m collected in this period; and
- Of the submitted preferential claims, 98% have been reviewed and admitted. However only 51% of the former employees have submitted a preferential claim. Efforts are being made to trace unresponsive former employees, who may have changed their address.

Issues and Challenges

The challenges to be faced by the HR workstream will be to maintain the right level of resource to meet the evolving requirements of the Administration’s as objectives are met and workforce requirements reduce. Clear and open dialogue with the employee group is key.

Additional challenges for the next six months are:

- Retaining key employees;
- Maintaining employee focus through a period of change; and
- Pursuing former employees for claims and commencing with payments in respect of preferential claims admitted.

Pensions

There have been no developments in relation to the claim for £119m submitted by the Trustees of the Lehman Brothers Pension Fund in respect of the deficit in the Scheme. However, work is in progress seeking to establish whether LBL may be able to make recoveries in respect of the Trustees’ claim from affiliate companies which benefitted from the employment of members of the Fund.

2.2 Corporation Tax and VAT

Overview

As Group Paying Agent of the Lehman UK tax Group and representative member of the VAT Group, LBL played an important and complex role in the Lehman UK tax affairs.

The primary objective of the tax team is finalising the timely repayment to the Group of up to £466m (excluding interest but subject to Crown set-off) of corporation tax.

Other key objectives include:

Compliance

- Ensuring tax compliance and statutory filing obligations are met.

Planning

- Minimising tax leakage from the UK Group.

HMRC Relationship

- Continuing to maintain a good relationship with HMRC to facilitate a pragmatic resolution of issues.

Progress

Specific progress in the period includes:

Corporation Tax

- To date, corporation tax repayments of £378m (including interest) have been received by LBL on behalf of the Group, of which £12m was received in the six months ended 14 September 2012;
- Two corporation tax repayments remain outstanding which may be subject to Crown set-off – whereby they will be reduced by other tax liabilities (e.g. PAYE) due to HMRC;
- Submission of 2010 Group loss position to HMRC, ensuring, by efficient usage of Group losses, no Group corporation tax liability in 2010; and
- Finalising 2011 accounts to enable preparation of 2011 tax returns to commence.

VAT

- LBL is part of a VAT group for which it is the representative member. All group VAT returns have been submitted up to the quarter ending May 2012. The August 2012 VAT return has been drafted and will be submitted shortly.

- LBL is due a VAT repayment of £470k for the November 2011, February 2012 and May 2012 quarters.

PAYE

- Several meetings have been held with HMRC to finalise agreement of the amount due to HMRC in respect of employment taxes to the date of Administration. Agreement now appears close and a further meeting is planned to finalise the amount and to discuss potential set off implications.
- With regards to the Employment Benefit Trusts, HMRC have asked for further information given the recent focus on such payroll planning.

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

- Finalising and submitting to HMRC the 2011 corporation tax returns;
- In conjunction with HMRC, complete reconciliation and agreement of the pre-appointment employment tax liabilities. Once this is finalised HMRC will be in a position to release the two outstanding corporation tax repayments; and
- Projecting the 2012 taxable position of the Group, to determine the likelihood of tax leakage in 2012.

2.3 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 included 289 debtor and creditor balances between LBL and the rest of the Group representing, at book value, £1.2bn of receivables and £0.7bn of payables as at 15 September 2008. LBL has a high concentration of its overall Affiliate debtor balances (c.£1.1bn) in just 5 relationships. In addition LBL held guarantees from LBHI in respect of some claims against other group companies.

Progress

The Intercompany team has continued to make progress on a number of significant receivable balances:

- Pursuant to the Plan of Reorganisation of Lehman Brothers Holdings Inc ('LBHI') and the other Affiliates in US Chapter 11 proceedings ('the US Estates'), which became fully operational and binding on 6 March 2012, LBL received £11.1m (\$17.6m) in first distribution payments on 17 April 2012. The total recovery from these claims remains uncertain but is anticipated to be in the region of \$55m;
- Also pursuant to the settlement agreement with the US Estates, Lehman Brothers Luxembourg Investments SARL ('LBLIS') has agreed LBL's unsecured creditor claim in the sum of \$225m and the principal US creditor of LBLIS has agreed to subordinate its claim behind LBL's claim. The quantum of any recovery from this claim remains contingent on the recovery LBLIS makes on its intercompany receivable and other balances;
- LBL is engaged in discussions with the US Affiliates that are not in Chapter 11 proceedings ('the non-Debtor Affiliates') with a view to settling with a group of these Affiliates where cash is currently available for distribution. LBL's receivable balances from this group of Affiliates is c.\$9m; recovery, whilst difficult to predict accurately, is expected to be at least \$2m;

- LBL's largest claim, for c.\$1.2bn, is against Lehman Brothers Holdings Plc ('LBH Plc'), which is in Administration. LBH Plc has cash assets of c.£45m, and a possibility of some significant additional recoveries. LBL's overall recovery from LBH Plc remains difficult to assess at this stage; and
- LBL has submitted claims in the estate of Lehman Brothers Europe Limited and in the estate of LBIE and is currently in discussion with the Administrators of those estates.

The Intercompany team continues to proactively progress more than 100 smaller LBL Affiliate balances (out of c.250 identified at the commencement of the Administration) where there remains a reasonable prospect of future realisations, including engaging with the US Estates in relation to balances with smaller entities controlled by them and which are not subject to Chapter 11 or other insolvency proceedings.

2.4 Affiliate company relationships

Overview

LBL continues to provide data to overseas Lehman Affiliates under the terms of agreements designed to manage the risks, and to enable the costs of so doing (including a contribution to overheads) to be recovered. No new contracts have been entered into during the period and whilst there have been some further ad hoc requests, the number of new requests under the existing contracts has continued to decline. Considerable progress has been made in fulfilling the existing requests, notably in respect of the unstructured data and hardcopy documents for LB Bankhaus ('LBB').

Progress

LBHI

The Services Agreement with LBHI extends through to 16 December 2012. Only two unstructured requests have been made during the period, but LBHI has had continued access to nine IT applications. Total billing for the period amounted to £1.042m.

LBB

The data agreement with LBB was extended from 30 June to 30 September 2012 to allow completion of the unstructured and hardcopy projects which were ongoing. The request for 2008 email has now been completed. The request for 2007 email, and the hardcopy document project are both nearing completion, but a further short extension to the contract will be necessary to allow time for the resolution of queries. Total billing for the period amounted to £0.733m.

Issues and challenges

For LBL the release of data to other Lehman Affiliates is a risk management exercise, and the maintenance of a robust audit trail to show the work done is a significant challenge. LBHI is currently assessing its future requirements, but in the absence of further requests from Lehman Affiliates generally, this workstream will diminish over the coming months.

Section 3 Statutory and other Information

| | |
|---|--|
| <i>Court details for the Administration:</i> | High Court of Justice, Chancery Division, Companies Court - Case 7945 of 2008 |
| <i>Full name:</i> | Lehman Brothers Limited |
| <i>Trading name:</i> | Lehman Brothers Limited |
| <i>Registered number:</i> | 846922 |
| <i>Registered address:</i> | Level 23, 25 Canada Square, London E14 5LQ, United Kingdom |
| <i>Company directors:</i> | 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) |
| <i>Company secretary:</i> | M Smith, P Dave, ESE Upton (all resigned 25/01/2010) |
| <i>Shareholdings held by the directors and secretary:</i> | None of the directors own shares in LBL |
| <i>Date of the Administration appointment:</i> | 15 September 2008 |
| <i>Administrators' names and addresses:</i> | AV Lomas, SA Pearson, DY Schwarzmann, MJA Jervis and DA Howell, of PricewaterhouseCoopers LLP, 7 More London Riverside, SE1 2RT |
| <i>Appointer's name and address:</i> | High Court of Justice, Chancery Division, Companies Court |
| <i>Objective being pursued by the Administrators:</i> | 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). |
| <i>Division of the Administrators' responsibilities:</i> | 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. |
| <i>Details of any extensions of the initial period of appointment:</i> | The Court has granted an extension of the Administration to 30 November 2013. |
| <i>Proposed end of the Administration:</i> | 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. |
| <i>Estimated dividend for unsecured creditors:</i> | It is too early to estimate the likely dividend for unsecured creditors. |
| <i>Estimated values of the prescribed part and LBL's net property:</i> | There is no qualifying floating charge holder, so there will be no prescribed part. |
| <i>Whether and why the Administrators intend to apply to court under Section 176A(5) IA86:</i> | Not applicable as there is no prescribed part. |
| <i>The European Regulation on Insolvency Proceedings (Council Regulation(EC) No. 1346/2000 of 29 May 2000):</i> | 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 the Administrators have held with your Committee.

Members of the Committee are bound by a confidentiality undertaking as some of the matters the Administrators 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

During the period covered by this progress report, the Committee has approved remuneration of £1,517,950 which comprises 5,620 hours at an average hourly rate of £270 in respect of the period 1 November 2011 to 30 April 2012.

Remuneration approved by the Committee includes £684,674 for work performed for and recoverable from Affiliate companies.

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

| Global Grade | Total hours | Total (£) |
|--|--------------------|------------------|
| Partner | 37 | 34,044 |
| Director | 152 | 134,242 |
| Senior Manager | 362 | 171,158 |
| Manager | 808 | 316,904 |
| Senior Associate | 1,984 | 530,488 |
| Associate | 2,277 | 331,114 |
| Total | 5,620 | 1,517,950 |
| Less work recoverable from Affiliate companies | | (684,674) |
| Net charge to LBL | | 833,276 |

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 are ultimately subject to their approval. In the six-month period from 15 March 2012 to 14 September 2012 the Administrators drew remuneration of £1,517,950.

Part of the net charge to LBL reported in previous periods relates to work on corporation tax and VAT issues on behalf of the Group and has been partially recovered from other Group companies in this and earlier periods. In addition, the disbursements drawn in the six month period from 15 March 2012 to 14 September 2012 have been fully recovered from Affiliate companies.

It is likely that significant levels of activity will be sustained for some time, but the Administrators expect that costs will begin to reduce in the coming months.

Section 5 Receipts and Payments to 14 September 2012

| Amount in millions | As at 14 Sept 2012 | | | | As at 14 Mar 2012 | | Movement |
|---|--------------------|--------------|----------------|--------------|-------------------|------------------|----------------|
| | GBP | EUR | USD | CHF | Total in GBP | Total in GBP | |
| Receipts | | | | | | | |
| Contribution from third parties * | 141.0 | 0.6 | 11.3 | - | 148.7 | 148.0 | 0.7 |
| Building recharge receipts | 129.4 | - | - | - | 129.4 | 129.4 | - |
| Payroll recharge receipts | 434.3 | 0.1 | 57.1 | - | 470.7 | 445.9 | 24.8 |
| Other (including realisations and payments for other companies) | 105.3 | 2.3 | 27.5 | 0.2 | 124.8 | 109.5 | 15.3 |
| Tax related receipts | 458.4 | - | - | - | 458.4 | 437.7 | 20.7 |
| VAT received on invoices | 7.0 | - | - | - | 7.0 | 7.0 | - |
| Total receipts for period | 1,275.4 | 3.0 | 95.9 | 0.2 | 1,339.0 | 1,277.5 | 61.5 |
| Payments | | | | | | | |
| Building and occupancy cost | (178.5) | (0.3) | (62.8) | - | (218.7) | (218.7) | - |
| Payroll and employee costs | (450.9) | (2.8) | (45.2) | - | (482.0) | (457.2) | (24.8) ~ |
| Other costs and payments | (61.5) | (0.2) | (1.2) | - | (62.4) | (56.0) | (6.4) |
| Other advisors' costs | (1.3) | - | - | - | (1.3) | (1.3) | - |
| Legal fees | (9.7) | - | - | - | (9.7) | (9.7) | - |
| Administrators' fees | (16.2) | - | - | - | (16.2) | (15.0) | (1.2) |
| Return of Corporation Tax to group companies | (338.0) | - | - | - | (338.0) | (256.0) | (82.0) |
| VAT related payments | (73.4) | - | - | - | (73.4) | (73.4) | - |
| VAT paid on invoices | (7.9) | - | (1.4) | - | (8.8) | (8.7) | (0.1) |
| Intercompany transfer | (1.5) | - | - | - | (1.5) | (1.5) | - |
| Total payments for period | (1,138.9) | (3.3) | (110.6) | - | (1,212.0) | (1,097.5) | (114.5) |
| Inter-currency transfers | | | | | | | |
| Receipts from inter-currency transfers | 22.6 | 2.7 | 57.8 | - | 61.7 | 50.6 | 11.1 |
| Payments from inter-currency transfers | (31.1) | (2.4) | (43.1) | (0.2) | (60.7) | (49.3) | (11.4) |
| Net inter-currency transfers | (8.5) | 0.3 | 14.7 | (0.2) | 1.0 | 1.3 | (0.3) |
| Net cash position | 128.0 | - | - | - | 128.0 | 181.3 | (53.3) |
| Bank balances | | | | | | | |
| Bank of England | - | - | - | - | - | - | - |
| HSBC | 14.0 | - | - | - | 14.0 | 9.7 | 4.3 |
| Money Market Funds | 114.0 | - | - | - | 114.0 | 171.6 | (57.6) |
| Net bank balance | 128.0 | - | - | - | 128.0 | 181.3 | (53.3) |

* Includes elements of building & occupancy and payroll related recharges

~ Includes £0.1m of payroll costs attributable to Lehman Brothers Limited

GBP £ equivalent is for information purposes only.

Estate funds held on interest bearing accounts, excluding a contingent £1m held in non-interest bearing account

Rates used for conversion are Financial Times rates fixed on 14 March 2012.

1 USD = 0.6333 GBP

1 EUR = 0.8686 GBP

1 CHF = 0.7215 GBP

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