

LB RE Financing No.3 Limited – In Administration

Joint Administrators' progress report for the period
30 April 2009 to 29 October 2009

27 November 2009

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Section 1: Purpose of the Joint Administrators' progress report

Introduction

This is the second progress report by the Joint Administrators (the "Administrators") of LB RE Financing No.3 Limited ("LBREF3" or the "Company"), pursuant to Rule 2.47(3)(a) of the Insolvency Rules 1986.

This report provides an update of the work that the Administrators have undertaken and the progress made since our appointment, with particular focus on the progress made in the six months to 29 October 2009.

Objective of the Administration

The Administrators are pursuing the objective of achieving a better result for the creditors of LBREF3 as a whole than would be likely if LBREF3 were wound up (without first being in Administration).

The specific aims of this Administration are to:

- Protect and control the Company's assets, namely the B class notes in a Special Purpose Vehicle held by the Company;
- Maximise income from the assets;
- Identify future cash flows and secure payments for the benefit of the Company; and
- Maximise value for the Company at the time of sale or transfer of the assets.

Creditors' Committee

There were insufficient nominations to enable the formation of a Creditors' Committee.

Outcome for creditors

At this time the Administrators are unable to provide a reliable estimate of the likely dividend to ordinary unsecured creditors as there are uncertainties regarding future realisations. The timing and level of any dividend, therefore, remains uncertain.

Extension of the Administration

On the application of the Administrators, the High Court made an Order extending the period of the Administration to 30 November 2010.

Future reports

The Administrators' will next report to creditors in approximately six months time or when the Administration comes to an end, whichever is sooner.

Signed:
For and on behalf of the Company



DA Howell
Joint Administrator
LB RE Financing No. 3 Limited

Section 2: Joint Administrators' actions to date

Overview

The Company was established as a vehicle in which to hold the Lehman Group's interest in loan notes issued by a number of off-balance sheet Special Purpose Vehicles ("SPV's"). The underlying assets in these SPVs are commercial mortgage backed securities. The Company was financed by Lehman Brothers Holdings, Inc ("LBHI") via its immediate parent companies.

Originally assets held by the Company in SPVs had a combined book value of c\$6billion. However in May 2008 c\$4.9billion of these assets were financed to Bankhaus and then in turn to a third party institution. The only asset held by LBREF3 on the date of appointment was a B note (the "B Note") in an SPV ("the SPV"), with a notional value of c\$1.1billion. The A Note in the SPV is held by a third party institution ("the A Note Holder") which acquired it as part of the financing arrangement with Bankhaus mentioned above.

Administrators' actions to date

The Administrators contacted the relevant stakeholders in relation to LBREF3's holding of a B Note in the SPV. This included the SPV's, Trustees, Servicer and Collection agent. The Administrators decided to hold the B Note and collect quarterly interest payments in respect of the B Note. The Administrators also made contact with the A Note Holder.

The Administrators have retained Lehman staff to assist them in the management of the Company's interests in the SPV. Day to day management of all underlying positions in the SPV is undertaken by the SPV servicer. Where individual loans go into default the Servicer is required to get B Note direction on the appropriate work out strategy. Lehman staff have assisted the Servicer in several such cases and preserved value for the benefit of both the A and B Notes.

The Administrators have also assisted in the release of the security agent role performed by Lehman Brothers International (Europe) - in Administration, of several loan positions in the SPV.

In the first progress report it was noted that the Administrators presented a restructuring proposal to the A Note Holder. This was to address specific issues they had raised and to provide options as to how the A and B Note Holders could work together towards recovering value from these assets.

The Administrators have not yet agreed on any form of consensual restructuring of the SPV with the A Note Holder.

To date, no interest or principle payments have been received by LBREF3 in relation to the B Note holding. Therefore the Administrators are faced with two choices:

1. Stop all work on LBREF3 owing to the lack of funds to meet ongoing costs, or
2. Sell the B Note.

The Administrators have been approached by LBHI to enter into an arrangement granting LBHI day to day control of the B Note with an option to acquire it or the shares of LBREF3, if certain conditions are met. In return LBHI will provide LBREF3 with a loan of £1.6m to meet the costs of the Administration of LBREF3. The loan will be repayable only from proceeds that flow from the B Note. LBHI also agreed, at its discretion, to meet the funding requirements associated with the B Note. LBHI will be paid a management fee that will only become payable if sufficient proceeds flow from the B Note.

The Administrators have also received an offer of €250,000 from the A Note Holder to purchase the B Note outright. No further expressions of interest were received in relation to the B Note. Therefore the £1.6m LBHI loan provides the best option to maximise the return for the benefit of LBREF3's creditors.

The LBHI transaction was subject to the approval of the Chapter 11 Bankruptcy Court in New York, USA. The motion to approve this was heard without objection on 18 November 2009 and the final transaction documents have recently been completed.

Extension of the Administrations

On 28 July 2009 the Administrators made an application to Court to extend the period of the Administration. The Court made an Order extending the Administration until 30 November 2010.

The application was made for the following reasons;

- There are various matters in the estate that, in the Administrators' view, would be better dealt with in Administration;
- Entering into an insolvency process other than

Administration has the effect of breaking the Group of Companies for tax purposes. The Administrators are aware that there are potential tax losses within the Group of Companies which may have value to this estate, and which would be lost if the Company entered into another insolvency process; and

- The Administrators have not yet determined the most appropriate exit route from Administration.

Section 3: Statutory and other information

| | |
|--|---|
| Court details for the Administration: | High Court of Justice, Chancery Division, Companies Court - Court Case 9634 of 2008 |
| Full name: | LB RE Financing No.3 Limited |
| Trading name: | LB RE Financing No.3 Limited |
| Registered number: | 06454161 |
| Registered address: | 25 Bank Street, London E14 5LE, England. |
| Company directors: | Paul Anthony Sherwood |
| Company secretary: | Emily Sarnia Everard Upton |
| Shareholdings held by the directors and secretary: | The director does not own shares in LBREF3 |
| Date of the Administration appointment: | 30 October 2008 |
| Administrators' names and addresses: | DA Howell, AV Lomas and DY Schwarzmman of PricewaterhouseCoopers LLP, Plumtree Court, London EC4A 4HT |
| Appointer's name and address: | The directors of the Company, 25 Bank Street, London E14 5LE |
| Objective being pursued by the Administrators: | Achieving a better result for LBREF3's creditors as a whole than would be likely if LBREF3 were wound up (without first being in Administration). |
| Division of the Administrators' responsibilities: | Statement of Power for the purposes of paragraph 100(2) Schedule B1 to the Insolvency Act 1986. The Sole Director of LB RE Financing No.3 Limited (the "Company") has appointed AV Lomas, DY Schwarzmman and DA Howell of PricewaterhouseCoopers LLP, Plumtree Court, London EC4A 4HT as Joint Administrators of the Company. The Joint Administrators will act jointly and severally so that all functions may be exercised by any or all of them. |
| Details of any extensions for the initial period of appointment | The Court has granted an extension of the Administration to 30 November 2010. |
| 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 LBREF3's net property: | Not applicable as there is 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 these are the main proceedings. |

Section 4: Financial information

Administrators' remuneration

At the meeting of creditors which was held by correspondence on 6 January 2009, creditors resolved that the Administrators' remuneration be fixed by reference to the time properly given by them and the various grades of their staff. The Administrators were also authorised to draw their remuneration on account from time to time.

Attached as an Appendix, is a summary of the Administrators' time costs for the period 1 December 2008 to 31 October 2009, presented in accordance with Statement of Insolvency Practice 9 ("SIP 9"), together with a narrative of the work performed. We previously provided a time cost analysis for the period 30 October 2008 to 30 November 2008.

The SIP 9 summary shows that the total time costs for the period is £1,005,664 which represents 2,089.9 hours at an average hourly rate of £481.22.

The Administrators' have yet to draw any remuneration, and will only do so when funds are available.

Receipts and payments account

An account of the receipts and payments in the Administration to 29 October 2009 is set out in Section 5 of this report.

Section 5: Receipts and payments for the period ended 29 October 2009

| | As at 29 October 2009 GBP (£) | As at 29 April 2009 GBP (£) | Movements GBP (£) |
|------------------------------|----------------------------------|--------------------------------|----------------------|
| RECEIPT | | | |
| Loan from Group Company | 700 | 700 | - |
| Receipts Grand Totals | 700 | 700 | - |
| PAYMENT | | | |
| Statutory advertising | 539 | 539 | - |
| Bank charges | 40 | 40 | - |
| VAT paid | 81 | 81 | - |
| Payments Grand Totals | 660 | 660 | - |
| NET POSITION | 40 | 40 | |
| CASH BALANCES | | | |
| Bank of England | - | | |
| HSBC | 40 | | |
| Money market deposits | - | | |
| Total Cash | 40 | | |

Appendix: Summary of the Joint Administrators' time costs for the period 1 December 2008 to 31 October 2009

| Classification of work | PARTNER / DIRECTOR | | SENIOR MANAGER / MANAGER | | SENIOR ASSOCIATE | | ASSOCIATE / SUPPORT STAFF | | Total | |
|---|--------------------|----------------|--------------------------|----------------|------------------|---------------|---------------------------|---------------|----------------|------------------|
| | Hrs | £ | Hrs | £ | Hrs | £ | Hrs | £ | Hrs | £ |
| Asset Realisations | 606.5 | 365,002 | 583.7 | 258,929 | - | - | 0.1 | 10 | 1190.3 | 623,941 |
| Strategy and Planning | 54.4 | 41,343 | 292.2 | 129,910 | 27.3 | 7,779 | 47.6 | 7,796 | 421.5 | 186,828 |
| Accounting and treasury | 0.2 | 120 | 29.9 | 12,339 | 12.3 | 3,499 | 14.9 | 2,775 | 57.3 | 18,733 |
| Statutory, compliance and other workstreams | 20.3 | 13,845 | 300 | 132,795 | 42.1 | 12,437 | 42.1 | 7,744 | 404.5 | 166,821 |
| Tax and VAT | 10.8 | 6,311 | 5.5 | 3,030 | | | | | 16.3 | 9,341 |
| Grand Total | 692.2 | 426,621 | 1,211.3 | 537,003 | 81.7 | 23,715 | 104.7 | 18,325 | 2,089.9 | 1,005,664 |

The Joint Administrators' policy for charging for disbursements is:

| | | | |
|--|-----------------------------------|--------------------|--|
| <p>Photocopying is charged at 3p per sheet for creditors and bulk copying</p> <p>Mileage is charged at a maximum of 62p per mile (up to 2000cc) or 81p per mile (over 2000cc)</p> <p>All other disbursements are charged at cost</p> | | | Costs to date (£) |
| Total | | | - |
| Current charge out rates | Business Recovery Services | Specialist* | <p>The Administrators' remuneration has been fixed by reference to the time properly given by the joint administrators and their staff in attending to matters arising in the administration. The remuneration is to be paid as and when funds become available at the charge-out rates shown for the various grades of staff who may be involved in this administration</p> <p>*Specialist departments within PricewaterhouseCoopers LLP, such as Tax, VAT and Pensions, do sometimes charge a small number of hours, should we require their expert advice. Their rates do vary, however, the figures shown give an indication of the maximum rate per hour.</p> <p>In common with all professional firms, the scale rates used by the Joint Administrators from PricewaterhouseCoopers LLP may periodically rise (for example to cover annual inflationary cost increases) over the period of the Administration. Any material amendments to these rates will be advised to the creditors in the next statutory report.</p> |
| Grade | Max £/hr | Max £/hr | |
| Partner | 785 | 1,070 | |
| Director | 590 | 890 | |
| Senior manager | 450 | 810 | |
| Manager | 390 | 590 | |
| Senior Associate | 320 | 395 | |
| Associate / Support Staff | 200 | 200 | |

Appendix: Narrative of time costs

The following narrative summarises the work undertaken by the Joint Administrators and their staff during the period.

Asset realisations - £623,941

- Review of SPV loan position;
- Support of SPV servicer on defaulted positions; and
- Negotiation of loan agreement with LBHI.

Strategy and planning - £186,828

- Preparation of restructuring proposals for SPV A Note Holder;
- Meetings and correspondence with A Note Holder; and
- Correspondence with SPV and its supporting agents.

Accounting and treasury - £18,733

- Identification and release of SPV positions where LBIE is security agent;
- Review of interest coverage ratios to inform correspondence with SPV and its supporting agents; and
- Preparation of claims against debtors to meet various bar dates.

Statutory, compliance and other workstreams - £166,821

- Preparation of progress reports and fee analysis;
- Support the extension of the LBREF3 period of administration; and
- Management of case database and file.

Tax and VAT - £9,341

- Tax advice in relation to LBHI loan agreement;
- Tax advice in relation to LBREF3 VAT registration; and
- Preparation of tax comps for HMRC.