

**IN THE HIGH COURT OF JUSTICE OF THE ISLE OF MAN
CHANCERY DIVISION**

**IN THE MATTER of THE COMPANIES ACT
1931**

and

**IN THE MATTER of KAUPTHING SINGER &
FRIEDLANDER (ISLE OF MAN) LIMITED**

and

**IN THE MATTER of THE JOINT PETITION OF
KAUPTHING SINGER & FRIEDLANDER (ISLE
OF MAN) LIMITED and THE FINANCIAL
SUPERVISION COMMISSION dated the 9th
day of October 2008**

SECOND AFFIDAVIT OF DAVID C. LOVETT

I DAVID C. LOVETT of AlixPartners Limited, North Audley Street, London being sworn make Oath and say as follows:

1. I am the same David C. Lovett who has previously sworn an affidavit in this matter. As before, I am authorised by AlixPartners to make this Affidavit.

2. Where the statements contained within this Affidavit are within my own knowledge, they are true. Where the statements are derived from information given to me, I state the source of that information and the statements are true to the best of my knowledge, information and belief. Where I comment on the actions and intentions of the Isle of Man Treasury, I have the authority of the Treasury Minister so to do.
3. I refer to my first affidavit sworn herein, by way of background. Where defined terms were used in my First Affidavit, they shall be adopted and used herein.

Privilege & Confidentiality

4. To the extent that reference is made herein to documents not exhibited hereto (or information derived from such documents), those documents (or information) are either the subject of legal professional privilege (which is not intended to be waived hereby) or confidentiality obligations imposed upon AlixPartners by virtue of a Non-disclosure Agreement entered into with the Liquidators Provisional. Nothing contained herein, and in particular (but without limitation), the fact that such documents (or information) are referred to herein is intended to waive privilege or breach such confidentiality obligations.
5. To the extent that reference is made herein to advice provided to Treasury, such advice remains confidential and privileged and nothing contained herein is intended to waive such privilege or confidentiality.

Background

6. As stated in my First Affidavit, AlixPartners has been retained by the Isle of Man Treasury to assess the situation pertaining to KSFIOM and the impact of the appointment of a liquidator over KSFIOM, with, in particular, a view to investigating the possibility of an orderly wind down or restructuring of KSFIOM, as an alternative to a traditional liquidation.
7. On 27 November 2008, at the request of the Isle of Man Treasury, the Petition was adjourned until 29 January 2009, to permit AlixPartners to progress a review of the financial position of KSFIOM, with a view to formulating proposals (if any) for the restructuring of KSFIOM.

Treasury's Review of KSFIOM's Financial Position

8. Since 27 November 2008, the team from AlixPartners, assisted by lawyers from Gough & Co. has worked closely with representatives of the Liquidators Provisional, PricewaterhouseCoopers, to review, on a confidential basis, much of the core documentation underlying certain identified key asset categories, namely: (i) KSFIOM's loan book, and collateral (ii) certificates of deposit, and (iii) collateral provided as security for "repo" lending. Together with the cash at bank, KSFIOM's claim against Kaupthing Singer & Friedlander Limited ("KSFUK") and its contingent claim against Kaupthing Bank hf ("Khf") represent the vast majority of KSFIOM's asset book.
9. As regards the loan book and collateral, prior to 27 November 2008, an initial review was conducted at the request of the Treasury by The Royal Bank of Scotland ("RBS"). Following conclusion of the RBS review, members of the AlixPartners team conducted a further review of key loan files, assisted by Gough & Co., who conducted a detailed

review of the security documentation for those loans. AlixPartners also spoke in detail with senior management and loan officers at KSFIOM responsible for management of the loan book and relationships with borrowers. Due to the limited time available, the above reviews have principally focussed on high value loans reflecting approximately 50% of the loan book by value. Time has not permitted a detailed legal and business review of the entire loan book, but AlixPartners believe it is possible to extrapolate the conclusions reached in our review and form a broadly reliable opinion of the nature and quality of the loan book and its underlying security.

10. In addition to the loan book and related collateral, AlixPartners and Gough & Co. have considered and investigated with the assistance of the Liquidators Provisional and their legal advisors: (i) KSFIOM's position vis-à-vis certain certificates of deposit purchased by KSFUK for KSFIOM and (ii) the prospects for the realisation of certain stocks held by KSFIOM as collateral for certain "repo" transactions that it had entered into. It should be noted that, in respect of these items, our review has been restricted in terms of access to information and documentation due to issues of confidentiality and privilege.
11. Notwithstanding the foregoing, our review has permitted AlixPartners to form a broad independent view of the quality of KSFIOM's assets, its depositor base, challenges arising there from and to estimate a range of potential outcomes to model an alternative solution and advise our client on this basis. It should be noted however that there remain a number of key issues yet to be resolved, which could yet significantly impact potential asset realisations.

Depositors' Compensation Scheme

12. In conjunction with Gough & Co. and advocates for the Depositors Compensation Scheme Manager (the FSC), consideration has been given to the potential implementation of the Depositors Compensation Scheme ("DCS") in accordance with the Financial Services Act 2008 Compensation of Depositors Regulations 2008, which came into operation on 9 October 2008. This has been necessary to ensure that any scheme of arrangement proposed has the effect of putting depositors who would otherwise qualify for payment under the DCS in an ideally better and certainly no worse position under a scheme of arrangement (if proposed) than they would be in a winding up when they could make a claim under the DCS.

Conclusion from AlixPartners' Review

13. AlixPartners has concluded and has advised the Isle of Man Treasury that a scheme of arrangement (under s.152 of the Companies Act (1931)) could be formulated and proposed to the creditors of KSFIOM. Such a proposal is now under consideration, but remains subject to Treasury approval and, I believe, will require firm commitments of support from all interested parties, including, in particular, the Petitioners and the Liquidators Provisional.
14. The aim of such a scheme would be to (i) assure DCS equivalent payments, (ii) provide a streamlined claims process, and (iii) accelerate payments to creditors in a scheduled and structured fashion.
15. This would be achieved in the following ways:
 - i. there would be a single claims adjudication process (rather than parallel ones under DCS and in a liquidation);

- ii. there would be a pre-agreed schedule of assured payments replicating the level of payments that would be due under the DCS;
 - iii. there would be a top-up funding loan facility provided by Treasury and/or others which would be made available to the Scheme Administrators to make the assured payments, to the extent that KSFIOM's realised assets are insufficient to do so;
 - iv. the payment regime under consideration would seek to ensure that increasing numbers of small depositors (who would otherwise be entitled to claim under the DCS) are paid in full as each scheduled assured payment is made.
16. AlixPartners believe that such a scheme of arrangement would provide the simplicity and certainty, no doubt sought by depositors, together with liquidity for KSFIOM that may, in due course, result in its sale as a going concern.
17. Details of such a possible scheme of arrangement have been shared with the Liquidators Provisional, the FSC, and those advising them, on a confidential basis. Subject, of course, to seeing the detailed terms set out in a Scheme Document and Explanatory Statement, I understand that the FSC would be broadly supportive of a scheme of arrangement which would offer superior terms of recovery for creditors of KSFIOM than would a liquidation and activation of the DCS.
18. AlixPartners are now working with Gough & Co. to consider and seek to overcome various legal and practical impediments that may prevent such a scheme of arrangement being proposed.

19. The Petition herein is presently adjourned to 29 January 2009. I believe that prior to that hearing, certain key decisions and/or responses are required, namely:

- i. Treasury needs to determine the extent to which it would be prepared to fund (subject to approval by Tynwald) the proposed assured payments and consider what other means are available to it to improve the outcome for the creditors;
- ii. The FSC, as Petitioner and as DCS Scheme Manager, needs to confirm its support and preference for this alternative and pledge resources to co-develop the scheme of arrangement documentation;
- iii. The Liquidators Provisional need to confirm their support and preference for this alternative and pledge resources to co-develop the scheme of arrangement documentation;
- iv. Discussions with third parties who would otherwise be contributors to the DCS by way of levy need to be progressed with respect to the manner in which any top-up funding is to be provided;
- v. Feedback is required from creditors.

20. With respect to each of the above, certain discussions have already taken place on a confidential basis and I would propose that AlixPartners proceed to engage with them in more detailed discussions, so that the necessary responses are received prior to 29 January 2009. A further update will be provided to the Court and creditors at that time.

21. Should all the necessary positive responses set out above be received, I anticipate that Treasury would seek a further adjournment of the Petition for at least a further 60 days to provide time for all outstanding issues to be resolved, appropriate documentation to be prepared and the necessary application(s) to Court be made for the convening of a meeting of creditors to consider and vote upon the proposed scheme.

SWORN at London :

This 15th day of January 2009

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Before me:

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A-Commissioner for Oaths SOLICITOR:

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