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**KAUPTHING BANK HF.**

**CREDITORS' REPORT**

- March 2010 -

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**KAUPTHING BANK**

## Disclaimer

This report (including all subsequent amendments and additions) was prepared by the Resolution Committee ("ResCom") for the creditors of Kaupthing Bank hf. ("the Bank") for information purposes only and is not intended for third party publication, distribution or release, in any manner. It should give creditors an overview of the background, the current situation and the potential steps going forward. The additions and amendments to this report since the previously published versions of this report are intended to give the creditors information on recent developments but are not necessarily and should not be regarded as an exhaustive list of all developments which creditors may consider material. In preparing and updating this report, the Bank has not taken account of the interest of any particular creditor or group of creditors.

Where information in this report is based on information from third parties the Bank believes such sources to be reliable. The Bank however accepts no responsibility for the accuracy of its sources. Furthermore, without prejudice to liability for fraud, the Bank accepts no responsibility for the accuracy or completeness of any information contained in this report and, without limitation to the foregoing, disclaims any liability which may be based on the accuracy or completeness of this report, modification of the report or any use or inability to use this report. The Bank is under no obligation to make amendments or changes to this publication if errors are found, opinions or information change or upon the discovery of new information. The fact that the Bank has made certain additions and amendments does not impose any obligation on the Bank to make amendments or changes to this publication in respect of any other developments, errors or changes in opinion or information, regardless of whether such development or changes occur after or before the date of publication of the revised report. In respect of additions and amendments made to this publication, the Bank is under no obligation to draw such additions and/or amendments to the attention of the intended recipients of this report.

This report does not include an estimate of the likely level of recoveries for creditors. Very material uncertainties continue to exist regarding the timing and realisable value of assets and the eventual level of creditors' claims. The Resolution Committee wish to caution creditors against using the data in this report to estimate likely recovery as any such estimates are likely to be materially misleading. The actual realisable value of the Bank's assets and liabilities may differ materially from the values set forth herein. Factors which may lead to material differences include:

- (a) Resolution of issues regarding the quantum of claims
- (b) The realisation method(s) used over time
- (c) The impact of set off and netting including in connection with derivative contracts
- (d) Movements in currency exchange rates and interest rates
- (e) Prevailing market conditions when assets are sold

Nothing in this report should be relied upon by any person for any purposes including, without limitation, in connection with trading decisions relating to the Bank. Neither the Bank, the Resolution Committee, the Winding-up Committee, nor the Moratorium Supervisor accepts any responsibility for any such reliance.

This report is published in English and Icelandic. In case of any discrepancies between the content of the English and Icelandic version the English language version takes precedence.

The use of the Bank's material, works or trademarks is forbidden without written consent except were otherwise expressly stated. Furthermore, it is prohibited to publish material made or gathered by the Bank without written consent.

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# Contents

- 1. The Resolution Committee .....6**
  - 1.1 Appointment and approach .....6
  - 1.2 Structure and divisions .....7
    - 1.2.1 Internal committees .....8
    - 1.2.2 Divisions .....9
    - 1.2.3 External advisors .....10
  - 1.3 Timeline of events .....12
- 2. Financial analysis .....14**
  - 2.1 Estimated valuation of the Bank’s assets .....14
    - 2.1.1 Valuation methodology .....16
    - 2.1.2 Asset Valuation .....17
    - 2.1.3 Notes on the Asset Valuation .....18
  - 2.2 The Loan Portfolio .....27
    - 2.2.1 Overview .....27
    - 2.2.2 Loans under AM .....30
    - 2.2.3 NOA portfolio .....30
    - 2.2.4 Restructuring .....31
    - 2.2.5 Repayments and exits .....35
  - 2.3 Derivatives .....36
  - 2.4 Overview of the Bank’s branches and subsidiaries .....38
    - 2.4.1 Subsidiaries: Current status .....38
    - 2.4.2 Branches: Current status .....42
  - 2.5 Other Assets .....44
  - 2.6 Operating cost .....45
- 3. The Claiming Process .....46**
  - 3.1 The Winding-up Committee .....46
  - 3.2 Summary of lodged claims .....47
- 4. Legal status and process going forward .....49**
  - 4.1 The moratorium process .....49
  - 4.2 Overview of the moratorium legislation .....49
  - 4.3 Potential closing of the moratorium process .....50
  - 4.4 Icelandic composition legislation overview .....51
    - 4.4.1 Introduction .....51
    - 4.4.2 Composition Claims .....52
    - 4.4.3 Composition Proposal .....52
    - 4.4.4 Creditors’ Meeting to consider Composition Proposal .....52
    - 4.4.5 Legal Effect of Composition .....53
    - 4.4.6 Composition Agreement not approved or court confirmation rejected .....53
  - 4.5 Creditors’ meetings .....53
  - 4.6 Overall restructuring and distribution to creditors .....54
  - 4.7 Future communication with creditors .....56
- Appendices .....58**
  - A1 Meeting minutes: Creditors’ Meeting held 5 February 2009 .....58
  - A2 Meeting minutes: Creditors’ Meeting held 20 October 2009 .....59
  - A3 Exchange rates .....62
  - A4 Initial tasks of the ResCom .....63

## The Bank's Creditors' Report

During the moratorium period the Bank's Creditors' Report is compiled on a regular basis for creditors and will be available on the Bank's website, [www.kaupthing.com](http://www.kaupthing.com). It is for creditors and other interested parties to keep abreast of the main developments and achievements.

The structure of 2010 Creditors' Report has been amended from previously published 2009 reports. Some material has been broken up and deleted and other has been added and updated.

Further, the additions and amendments to this report since the previously 2009 published versions are intended to give creditors information on recent developments but should not be regarded as an exhaustive list of developments which creditors may consider material.

The major additions and amendments from the previously published report will be highlighted in blue text while all minor changes will be left as black text. Deleted text, which is not applicable anymore and none of which was significant, has been deleted without any notification to the readers and can be found in 2009 publications. Updates will continue to be published on the Bank's website to keep creditors informed of the latest progress of the Bank's operations. Further information on communications with creditors, can be seen in chapter 4.7 *Future communication with creditors*.

Readers' attention is drawn to the terms of the disclaimer concerning the content and the purpose of this report at the beginning and the end of the report.

## Abbreviations

The following abbreviations are used in this report:

FME	The Icelandic Financial Supervisory Authority
The ResCom	The Resolution Committee
ICC	Informal Creditors' Committee
The Bank, Kaupthing	Kaupthing Bank hf.
Arion Bank	Arion banki hf. (formerly New Kaupthing)
ICB	The Central Bank of Iceland
IMF	International Monetary Fund
The Disbursement Act	Act No. 125/2008 on the Authority for Treasury Disbursements due to Unusual Financial Market Circumstances etc.
The Transfer Decision	Decision of the FME on the disposal of assets and liabilities of Kaupthing Bank hf. to Arion Bank dated 21 October 2008
The Bankruptcy Act	Icelandic Act on Bankruptcy, etc., No. 21/1991
Act on Financial Undertakings	Act on Financial Undertakings, No. 161/2002, cf. Act No. 44/2009 and subsequent amendments.

# 1. The Resolution Committee

## 1.1 Appointment and approach

On 9 October 2008 Kaupthing Bank's board of directors resigned on its own initiative due to the Bank's financial difficulties and a Resolution Committee (the "ResCom") was appointed for the Bank by the FME in accordance with Act no. 125/2008 on the Authority for Treasury Disbursements due to Unusual Financial Market Circumstances etc. (the "Disbursement Act") passed in reaction to the collapse of the banking system in Iceland. The ResCom immediately assumed control of the Bank and wields all the authority of the Bank's board of directors. The role and duties of the Resolution Committee are laid down in the Act on Financial Undertakings, no. 161/2002, as amended by Act no. 44/2009 and subsequent amendments, ("Act on Financial Undertakings), also the Act no. 21/1991 on Bankruptcy etc. (the "Bankruptcy Act"). According to Act no. 44/2009 the ResCom was given power by law to represent the Bank in all matters, safeguard its interests and maximise asset value. The provisions of articles 102 and 103 of the Bankruptcy Act clearly state that the ResCom has a legal obligation to maximise the value of the Bank's assets and preserving the interests of the creditor body as a whole.

The ResCom was initially appointed by FME, which is an independent government entity, but the ResCom's independence has been enhanced with the enactment of Act no. 44/2009. The ResCom is comprised of two Supreme Court attorneys and two Certified Public Accountants, namely the following:

- Steinar Thor Gudgeirsson, Attorney to the Supreme Court of Iceland – Chairman
- Johannes Runar Johannsson, Attorney to the Supreme Court of Iceland
- Knutur Thorhallsson, Certified Public Accountant
- Theodor Sigurbergsson, Certified Public Accountant

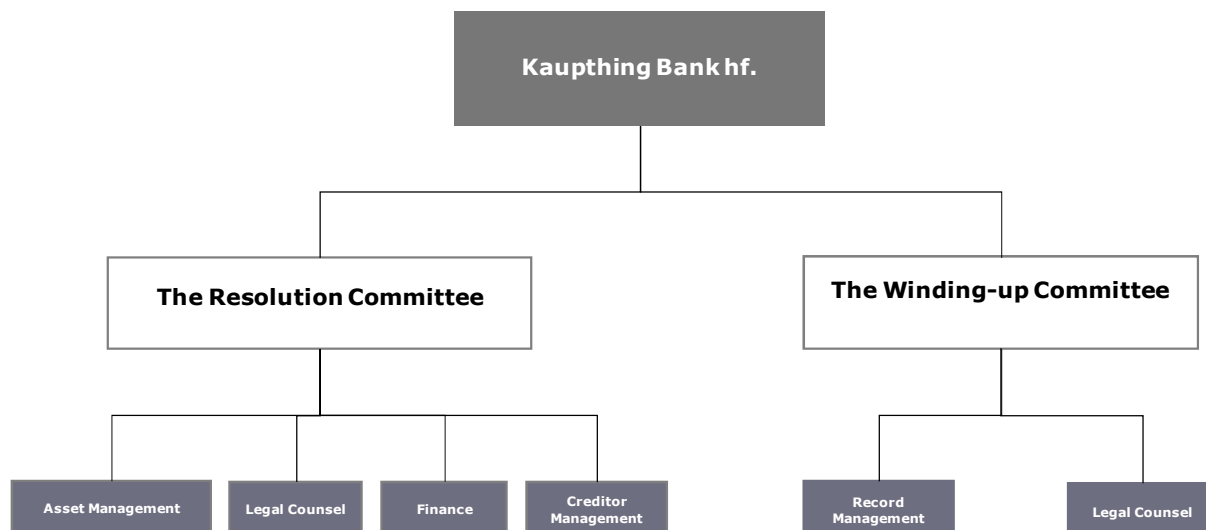
The ResCom handles the Bank's affairs, including directing its daily operations, ensuring assets are handled properly, concluding contracts and other legal instruments on its behalf, and safeguarding its interests to the utmost extent possible.

The ResCom's principal objective is to ensure proper handling of, and maximise the value of the Bank's assets to the benefit of its creditors and to return value to creditors as timely as possible.

In order to maximise the value of the Bank's assets, the Bank focuses on the following processes:

- Restructuring of nonperforming assets (loans, upside participation and taking equity positions) which was largely completed in 2009
- Monetisation of current asset pool through
  - Run-down over time
  - Collection of assets
  - Disposal of certain assets
  - Continuous monitoring of assets regarding optimal timing for exit and performance
- If beneficial and required, support of current assets through prolongation of current loans, equity injection or new loans (very restrictive)
- Litigation

On 25 May 2009, the Reykjavik District Court approved a request from the ResCom and appointed a Winding-up Committee for the Bank to handle the Bank's claims' process. The appointment was in accordance with the recent amendments to the Act on Financial Undertakings. In short, the ResCom is responsible for the asset side of the Bank and its daily operation, but the Winding-up Committee administers the formal process of filing claims, handles all claims against the Bank and makes decisions regarding their recognition.



*Organizational structure of the Bank.*

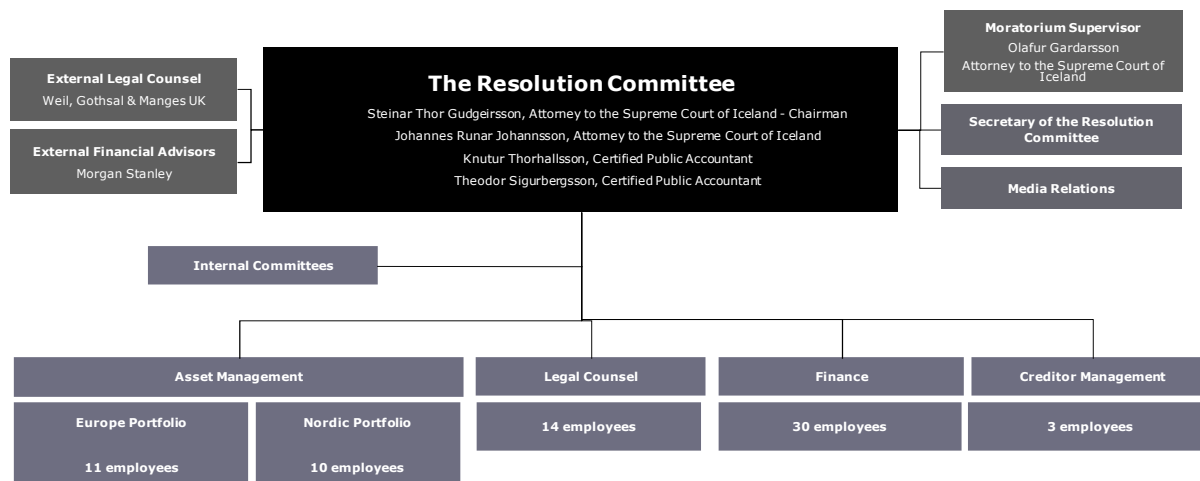
At the beginning the ResCom was up against major challenges where many borrowers were in great turmoil because of the Bank's status and the collapse of 85% of the banking system in Iceland. The main task was to stabilize the situation and to retain value wherever possible by preventing the collapse of different assets and by refusing strongly any fire sale bids. Assets were saved and transferred from branches and a subsidiary in the Nordic region to the Bank. Despite difficult circumstances in the beginning, these objectives were achieved.

Other tasks the ResCom worked on in the beginning, and have been completed, include: maintaining the Bank's commercial banking operations in Iceland, protecting depositors both domestically and overseas in accordance with the Disbursement Act, and ensuring cash flow in all currencies both domestically and to/from foreign jurisdictions.

## 1.2 Structure and divisions

In order to perform its primary duties and to achieve its objectives, the ResCom must possess the requisite expertise to manage the assets and to provide the necessary services. Therefore the ResCom has hired experts in various fields to manage the Bank's assets, which include the loan portfolio, derivatives, securities and foreign subsidiaries and branches.

Four divisions have been created which report to the ResCom and each division is headed by a managing director responsible for the operation of that division. The ResCom holds weekly update meetings with the management team to review and discuss recent and overall progresses and highlights. The ResCom also retains external advisors to ensure that creditors' interests are served at all times.



The ResCom's structure.

### 1.2.1 Internal committees

In addition to the four divisions and to further strengthen the infrastructure and the operations of the Bank, several working committees have been established. The ResCom or its sub committees hold regular meetings each working day and work within formal guidelines and procedures to resolve the tasks at hand.

The *Asset Committee* was established shortly after the date of the ResCom's appointment and has the role of both credit committee and investment committee in a traditional financial institution. The Asset Committee holds two regular meetings each week. It comprises two members of the ResCom and three managing directors of the Asset Management team. All credit related decisions are referred to the Asset Committee. All major decisions of the Asset Committee are referred to the ResCom for approval. The ResCom makes the final decision whether to approve or decline a request.

The *Finance Committee* is responsible for the Bank's finances. Its main role is to formulate the finance division's strategy in terms of book-keeping and accounting procedures. The committee comprises two members from the ResCom and the managing director of Finance. The committee is responsible for all financial disclosure both externally and internally to the ResCom and its sub-committees. The Finance Committee defines which guidelines the Bank adheres to, both with respect to accounting rules and international standards and internal work procedures. The committee develops and oversees the execution of budgetary plans. The committee is also responsible for management of cash and cash equivalents.

The *Inspection Committee* has the role of reviewing certain transactions and to prepare and commence legal proceedings against parties that might be in debt to the Bank due to those transactions, or are alternatively responsible for potential loss of the Bank resulting from the transactions. The aim is, in other words, to realise all possible claims which the Bank might have against third parties in relation to the specific transactions mentioned above, including claims arising from unusual action by the former management of the Bank or third parties. The committee comprises two members from the ResCom. This committee is also responsible for all correspondence and communication with the Special Investigation Commission ("SIC"), operating under the provision of Act No. 142/2008, the FME and the Special Prosecutor, operating under the provision of Act No. 135/2008.

The *Set-off and Netting Committee* is responsible for preparation of netting and set-off cases, collection of claims deriving from derivative contracts and related matters. The Set-off and Netting Committee consists of one member from the ResCom, one member from the Winding-Up Committee and the managing director of Legal. The committee was originally established in February 2009 but was re-established in the beginning of June 2009 following the appointment of the Winding-up Committee. The participation of the Winding-up Committee is needed for the set-off process, as its

current role is to evaluate all claims brought against the Bank, including claims that might be used for set-off.

## 1.2.2 Divisions

### **Asset management**

The role of the unit is to develop the Bank's asset pool of loans and securities with the ultimate goal of securing maximum recovery from these assets. This is done by pro-active management of every asset, maintaining a cash flow plan for the Bank's loan portfolio which is updated regularly; by assessing the capital requirements of the asset portfolio and the Bank's capacity to meet this. [The Bank's loan to customers portfolio consists of more than 113 borrower groups and the total outstanding notional is around ISK 451bn at fair value as at 31 December 2009, all of which have a designated account manager who is responsible for them.](#)

There are 21 employees in this division, most of whom are highly experienced in the investment & corporate banking field with up to 17 years experience in the industry from international reputable financial institutions. The team comprises specialists with diversified background and experience, both domestically and internationally, across corporate finance, corporate banking, private equity, leverage finance, operational and capital restructuring and workouts supported with a team of legal specialists with extensive experience across all legal aspects of banking transactions. Some members of staff have worked on both sides of the fence, that is whilst employees or managers of respective businesses and also from the banking side.

The specialists in the asset management division lead the projects internally and the process is supported by an external advisory service as needed. Tasks where the asset management has engaged with external advisers include corporate finance advisory, due diligence reports, business verification, tax planning and appraisal and valuation.

It is expected that the asset portfolio will be self-financing and instalments and interest payments on the loans will be sufficient to support other assets if needed. Furthermore, it is expected that in the current environment fees generated from the loan portfolio will cover the costs of running the asset management division.

### **Legal counsel**

The legal counsel division provides support and legal advice to the ResCom in general as well as in individual projects, such as the capitalisation of Arion Bank and the closure and winding down the subsidiaries and branches of the Bank. This division comprises legal experts with extensive knowledge in financial legislation, the Icelandic bankruptcy legislation and corporate law in general. In addition, the division provides support and legal advice to all the other divisions within the Bank as needed. Responsibility for each account in the loan portfolio has been allocated and employees of the team are involved in the legal aspects of all transactions. The legal counsel division works with the Bank's external legal counsel with respect to the foreign derivatives portfolio and leads the legal work stream with respect to the Icelandic derivatives portfolio. The division is responsible for collection of claims and preparation for litigation both domestically and internationally in collaboration with external legal counsel. The division furthermore works together with external advisers on investigation and recovery in regard to unusual transactions. The division supervises the hiring of outside legal experts, both in Iceland and abroad, and monitors the quality of the work they provide and has an overview of expenses incurred by external legal advice.

### **Finance**

The division is responsible for executing all aspects of the Bank's finances according to guidelines provided by the Finance Committee which is a sub-committee of the ResCom. The finance division has four sub-divisions:

*Accounting and Reporting* which is responsible for all accounting procedures. The unit prepares financial statements which are issued in the Creditors' Report semi-annually as well as other reports more frequently for internal purposes.

*Portfolio management* ("PM") manages and monitors specific asset classes on the balance sheet, in some cases in co-ordination with the asset management function. The unit is split into three sub-units:

- *PM – Loans*, works closely with the asset management unit. The team monitors, analyses and manages all loans and matters related to them in co-operation with the respective account managers. This entails tasks like loan administrative matters, collateral analysis, covenant monitoring, cash flow projections, credit risk analysis, internal and external reporting etc.
- *PM – Cash and securities*, analysis and monitors the bank's bonds and equity stakes as well as managing the cash reserves of the bank.
- *PM– Subsidiaries and other assets*, analysis the bank's subsidiaries, branches and other assets categories on the balance sheet.

The portfolio management unit co-operates extensively with the accounting and reporting unit in preparation of the annual accounts

*Operations* is responsible for day-to-day operations, records management, and human resource matters.

*Derivatives* is responsible for valuations of outstanding unsettled derivative trades and management of open trades. In addition, the unit is responsible for the preparation of settlement notices to counterparties and other back office functions in relation to the settlement of the derivatives book.

### **Creditor Management**

Creditor Management is responsible for relations with creditors and in addition has supervised communications with the Informal Creditors' Committee ("ICC"). The team manages the relationship with Morgan Stanley, the Bank's financial advisor, and is involved in their main projects, including the the capitalization agreement on Arion Bank with the Ministry of Finance and the restructuring of the Bank.

The website, [www.kaupthing.com](http://www.kaupthing.com), maintained and updated by the creditor management, is a source where creditors, the media, authorities and other parties can access regular updated information about the Bank. Interested parties can send questions, read the latest announcements and updates and can keep abreast of the main developments since 9 October 2008. The website has been updated to include material relating to the Winding-up Committee. The users of the website can subscribe to news and updated material, such as new updates of the Creditors' Report.

The publication of the list of lodged claims presented a good opportunity to reorganise creditor communications and introduce new processes for information disclosure. The Creditors' Report will continue to be published on regular basis on the Bank's website to keep creditors informed of the latest progress of the Bank's operations.

Additionally, there will be quarterly (or event-driven) Creditors' Report Update Meetings with dial-in opportunity for creditors. Questions will have to be sent in advance. The first such meeting is scheduled 15 March 2010. More information can be found on the Bank's website and in chapter 4.7 *Future communication with creditors*.

Creditors are invited to ask questions in advance, by sending an e-mail to [creditorcontact@kaupthing.com](mailto:creditorcontact@kaupthing.com). Every effort is made to respond to questions received prior to the creditors meetings if the relevant information is available. However, for multiple reasons, including bank secrecy and commercial sensitivity, information on certain matters cannot be disclosed.

### **1.2.3 External advisors**

To uphold utmost professional standards, and in line with wishes from many of its largest creditors the ResCom deploys necessary expertise in every aspect of its operations. This entails hiring various external experts for advice on numerous on-going or stand-alone projects. Morgan Stanley is the ResCom's external financial advisor. Amongst projects, they have advised and assisted with, is the negotiation with the Ministry of Finance and resulting agreements on the capitalization of Arion Bank.

Furthermore, throughout the due diligence and negotiation process the Bank used advisors as deemed necessary including Morgan Stanley, Weil, Gotshal & Manges UK, Lex and Deloitte Iceland.

Currently, Morgan Stanley is leading the overall restructuring work of the Bank itself and the formulation of composition proposals that may be presented to creditors at a later stage. Weil, Gotshal & Manges UK is the main external legal counsel on litigation and recovery proceedings. Alvarez and Marsal has been retained to manage the overall process of the winding down of the derivatives book and execute a plan that will maximise recoveries. Furthermore, the business law firm Olswang was appointed as an external legal counsel to work on the legal process associated with recoveries of the derivatives portfolio. Capacent and PwC Iceland have been engaged to assist in valuation and accounting. The ResCom has hired a forensic team from Grant Thornton UK to examine voidable measures focussing particularly on possible rescissions and damages claims in relation to foreign parties. The Winding-Up Committee has engaged PwC Iceland to do the same for domestic parties.

In all of the major restructuring cases, the Bank has hired external advisors. Depending on the nature of the restructuring projects, these external parties can be financial advisors, legal counsels, real estate consultants, retail experts, accountants, auditors, etc. The cost of these is in most cases paid by the respective borrower.

In addition to the experts already mentioned, the following parties have been engaged in resolving and working on various legal matters for the Bank:

- CHSH Cerha Hempel Spiegelfeld Hlawati and WOLF THEISS in Austria
- Plesner and Holts in Denmark
- Borenius, Maples and Hannes Snellman in Finland
- Herbert Smith and Allen & Overy in France
- Heuking Kühn Lüer Wojtek in Germany
- Simmons & Simmons in Hong Kong
- Juris, Lex, Landslog Law Offices and Fulltingi in Iceland
- Studio Legale Canelutti in Italy
- Molitor, Fisch & Associates, Kleyr, Grasso and Associates in Luxembourg
- Wiborg Rein in Norway
- Cuatrecasas and Goncalves Pereira in Spain
- Winge, Mannheimer Swartling, Lindahl and Frank Advokat, in Sweden
- Allen & Overy and Loyens & Loeff in the Netherlands
- DLA Piper, Slaughter and May, Hammonds, Olswang, Smith&Williamson, Rosenblatt, Heatons, Sidley Austin and Allen & Overy in the UK
- Nixon Peabody and John Day in the USA

Tasks, where the asset management has engaged external advisers include corporate finance advisory, due diligence reports, business verification, tax planning and appraisal and valuation.

- KPMG, advice on restructuring in Denmark
- Deloitte, tax advice and structuring in Finland
- PwC, valuation and business sensitivity study in Finland
- Pareto, valuation in Norway
- PwC, advice on restructuring in Sweden
- Capacent, advice on restructuring and valuation in Sweden
- Catella, advice on restructuring in Sweden
- Earnst & Young, tax advice in Sweden
- Newsec, real estate advice in Sweden
- BDO Stoy Hayward, advice on tax and restructuring and valuation in the UK
- Deloitte, valuation in the UK
- PwC, advice on tax and restructuring and business valuation in the UK

### 1.3 *Timeline of events*

#### **6 – 9 October 2008**

- Icelandic parliament passes the Disbursement Act
- FSA in the UK succeeds in having administrators appointed over KSF
- The Bank's board of directors requests that the FME take control of the Bank pursuant to the Disbursement Act

#### **9 October – 22 October 2008**

- FME appoints a ResCom which immediately assumes control of the Bank
- Arion Bank is established
- Certain domestic assets and domestic deposits transferred to Arion Bank in accordance with the decision of the FME on the disposal of assets and liabilities of Kaupthing Bank hf. to Arion Bank dated 21 October 2008 ("The Transfer Decision")

#### **22 October 2008 – 30 December 2009**

- The ResCom establishes communications with creditors for consultation and feedback
- Moratorium granted and Olafur Gardarsson appointed as the Moratorium Supervisor
- Moratorium is recognized as a foreign main proceeding under Chapter 15 of the US Bankruptcy Code
- Morgan Stanley appointed as a financial advisor to advise and assist on restructuring the Bank
- Creditors' Meeting convened by the Moratorium Supervisor on **5 February 2009**
- Moratorium of the Bank extended by the District Court of Reykjavik to **13 November 2009**
- Important amendments made to the Act on Financial Undertakings on **22 April 2009**
- The Bank's Winding-up Committee appointed on **25 May 2009**
- The formal claim process started on **30 June 2009** and last for 6 months.
- **On 20 July 2009**, the agreement between the ResCom and the Government on the capitalization of Arion Bank announced
- **On 14 August 2009**, the Government capitalized Arion Bank with approx. ISK 72bn in common equity which allows Arion Bank to function as a fully operational bank
- **On 3 September 2009**, the Bank's ResCom and the Government signed an agreement on settlement between the Bank and Arion Bank in accordance with the agreement announced on 20 July 2009
- A creditors' meeting held on **20 October 2009** to discuss the agreement between the ResCom and the Government on Arion Bank and to discuss the possible extension of moratorium on debt payments.
- **On 13 November 2009** a nine months extension of moratorium was requested at the District Court of Reykjavik. The Bank was granted an extension of moratorium on debt payments until 13 August 2010

- **On 1 December 2009**, the ResCom announced it would acquire 87% share in Arion Bank
- **On 30 December 2009**, the formal claim registration process ended

#### ***1 January 2010 to date***

- **On 11 January 2010**, FME granted the Bank's subsidiary Kaupskil ehf. permission to own a qualifying holding in Arion Bank on behalf of Kaupthing.
- **On 22 January 2010**, the list of claims made available to creditors
- **29 January 2010**: Creditors' Meeting held at 10:00 a.m. at Hilton Hotel Nordica

#### ***Next steps***

- **15 March 2010**: Creditors' Report Update Meeting in London
- **18 May 2010**: Creditors' Meeting from 29 January 2010 continued
- **24 November 2010**: Maximum moratorium period for the Bank ends. The Bank will, upon the conclusion of the moratorium, automatically enter into winding-up proceedings. According to the recent amendment of the Act on Financial Undertakings, the Bank's protection against litigation, enforcement, collection measures and other depletion of assets obtained under the moratorium will continue to exist when the Bank formally enters a winding-up process.

## 2. Financial analysis

### 2.1 *Estimated valuation of the Bank's assets*

The financial information in this subchapter as at 31 December 2009, 30 June 2009 and 31 December 2008 was prepared by the ResCom and employees of Kaupthing Bank with the assistance of external advisors where appropriate for Kaupthing Bank hf., the parent company. The financial information is neither audited nor reviewed by independent auditors but PricewaterhouseCoopers hf. in Iceland has performed agreed upon procedures in various accounts regarding reconciliation, valuation methods and review of impairment. The financial information is presented in Icelandic krona ("ISK"), rounded to the nearest million.

The ResCom emphasizes that the valuation herein is a historic valuation only, and one which only takes into account the Bank's current strategy, to safeguard and increase the value of the Bank's assets achieved to 31 December 2009 and not thereafter. No attempts were made to assess the possible future value of assets, or to estimate likely recovery of creditors' claims. Whilst significant data is included in this report, readers are cautioned against estimating the likely level of recoveries as material uncertainties exist regarding, inter alia, the level of realizations and eventual level of recognized claims.

A formal process for the creditors of the Bank to file claims against the Bank began on 30 June 2009 and ended on 30 December 2009. Until the Winding-up Committee has recognized all claims and disputes have been settled, the real and accurate amount of liabilities is uncertain. According to Act no. 44/2009, all claims should have been filed as at 22 April 2009 in the relevant currency and converted into ISK at the exchange rate published by the Central Bank of Iceland on 22 April 2009. Hence, the liability side has been fixed in ISK as at that date for all relevant claims.

The estimated liability side fixed as at 22 April 2009 was published in the Bank's half year accounts as at 30 June 2009. The claim registry was published by the Winding-up Committee as at 22 January 2009. In this subchapter, the ResCom has roughly categorized the claim registry in order for it to be comparable with the previously published liability side of the balance sheet as at 30 June 2009. Revision of claims which had been fixed as at 22 April 2009 was not carried out since the responsibility of determining the liability side of the balance sheet is placed with the Winding-up Committee through a strict legal process set out in Act no. 161/2002 on Financial Undertakings and Act no. 21/1991 on Bankruptcy etc.

In preparing the financial information in this report, the Bank has placed emphasis on ascertaining the value and correct accounting of the assets of the Bank. The liabilities of the Bank are however currently being determined through a formal claims filing process which is administered by the Winding-up Committee of the Bank. The scope of the liabilities of the Bank remains uncertain until the legal process of recognizing and rejecting claims has been further progressed by the Winding-up Committee. In the event there are discrepancies between the liabilities estimate presented by the Resolution Committee and the claims against the Bank as finally determined by the Winding-up Committee, the determination of liabilities by the Winding-up Committee prevails.

The Bank continues work on further confirming and ascertaining earlier accounting of the Bank's assets. In some cases however, the data and information used in this work is incomplete or insufficient. In such cases the Bank has used best efforts and cautious valuation methods in determining asset value. Due to the aforesaid, some discrepancies are inevitable when comparing earlier and more recent financial statements published by the Bank. The Bank endeavours to use the most accurate information available at any given time for the preparation of financial information and reserves the right to make any necessary amendments to the financial information from time to time to reflect any changes.

The valuation of assets does not fully take into account the impact of set-off. Set-off impact could clearly make a material difference to overall creditor recoveries. Further information on set-off is provided in note 24. Further information will be provided on this matter as it becomes available.

As noted in this report's disclaimer, the actual realisable value of the Bank's assets and liabilities may differ materially from the values set forth herein. Factors which may lead to material differences include:

- (a) Resolution of issues regarding the quantum of claims
- (b) The realisation method(s) used over time
- (c) The impact of set off and netting including in connection with derivative contracts
- (d) Movements in currency exchange rates and interest rates
- (e) Prevailing market conditions when assets are sold

The financial information as it appears may be a redacted version and should be viewed as such.

Readers' attention is drawn to other terms of the disclaimer at the beginning and the end of this report.

## 2.1.1 Valuation methodology

The valuation methodology for each asset class is abbreviated below .

Cash in hand	The balance of all cash accounts as at 31 December 2009 without any discount.
Loans to and claims against credit institutions	Loans to and claims against credit institutions are valued at fair value. Estimated credit risk of the counterparty has been taken into account in provisions for losses.
Loans to customers	<p>Loans to customers are valued at fair value. The fair value is based on market transactions where possible or recognised valuation techniques. Valuation techniques include comparison to market prices of similar observable instruments, comparison to similar instruments for which market observable prices exist, valuations of underlying collateral, net present value techniques, and third party valuations where again different valuation models are taken into account. Small exposures where individual loans have carrying value of less than ISK 2 billion can be valued based on categorisation and multiples at certain intervals.</p> <p>Loans transferred to Arion Bank as part of Arion Bank's capitalization (see further in note 21) are valued at the transfer price.</p>
Bonds and debt	<p>Listed and liquid: the market value as at 31 December 2009.</p> <p>Unlisted and listed illiquid: similar valuation methodology was applied to this category as in Loans to customers at fair value. Illiquidity discount was applied to less liquid positions.</p> <p>Pledged positions: the pledged positions are now represented at the assumed market value of the underlying collateral as at the Bank's interpretation of the valuation date of the underlying agreements.</p>
Shares and instruments with variable income	<p>Listed and liquid: the market value as at 31 December 2009</p> <p>Unlisted and listed illiquid: similar valuation methodology was applied to this category as in Loans to customers at fair value. Illiquidity discount was applied to less liquid positions.</p> <p>Pledged positions: the pledged positions are now represented at the assumed market value of the underlying collateral as at the bank's interpretation of the valuation date of the underlying agreements.</p>
Derivatives and unpaid derivatives	<p>This category includes both live trades as well as terminated trades. Terminated trades are converted to relevant termination currency as at the termination date.</p> <p>The calculated amount of derivatives before provisions is based on the Bank's own valuations, which may differ from the final settlement amounts. When determining the value of more complex derivatives and structured products, the Bank is using the services of a leading independent company which specializes in derivative valuations and risk management services. Derivatives with the same legal entity are netted.</p> <p>Most of the derivatives are not quoted in active markets but in that case the valuation is based on quoted prices. A market is considered active if quoted prices are readily and regularly available and those prices represent actual and regularly occurring market transactions on an arm's length basis. For all other derivative assets fair value is determined by using valuation techniques. The Bank uses widely recognised valuation models for the common and simpler derivatives like options and interest rate and currency swaps. For more complex instruments, the Bank uses proprietary models, which usually are developed from recognised valuation models. Some of the inputs into these models may not be directly observable from market data but are commonly derived from market observables, e.g. from market prices or rates.</p> <p>Default valuation rules under the ISDA framework generally favour the non-defaulting counterparty which may result in adverse effect on the value of the derivatives. Once ISDA derivative contracts have been terminated the non-defaulting counterparty must determine the net amounts owed by or to the defaulting counterparty. Close-out notices providing details of such calculations enable the Bank to reconcile amounts. In many cases, either no close-out statement has been received or has been inadequately detailed. Some provisions were made to the Bank's valuation of ISDA derivatives to account for potential disputes in valuation. For Non-ISDA counterparties, a significant valuation adjustment was made on derivative assets to account for credit, liquidity and collateral risk associated with each counterparty.</p> <p>Foreign exposures in this category are converted to ISK as at the date of this account, 31 December 2009.</p>
Investments in subsidiaries	Investments in subsidiaries are valued at net asset value or the enterprise value which is generally the estimated fair value as at 31 December 2009 except for FIH which is shown as fully pledged against a loan with the Central Bank of Iceland at the estimated current value of the obligation.
Other assets	Other assets are valued at fair value. Estimated credit risk of the counterparty has been taken into account in provisions for losses.

## Asset Valuation

### 31 December 2009

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	Notes	31.12.2009	30.6.2009	31.12.2008
<b>Assets</b>				
Cash in hand .....	1-2	176.066	98.799	77.963
Loans to and claims against credit institutions .....	3-4	323.267	442.923	522.714
Loans to customers .....	5-12	450.948	439.521	337.023
Bonds and debt instruments .....	13-14	63.025	119.064	115.931
Shares and instruments with variable income .....	15-16	178.379	214.600	161.851
Derivatives and unpaid derivatives .....	17-18	239.017	246.073	233.862
Investments in subsidiaries .....	19	141.626	135.562	129.464
Other assets .....	20	7.540	9.102	13.361
<b>Total Assets</b>	1-20	<u>1.579.868</u>	<u>1.705.644</u>	<u>1.592.169</u>

## 2.1.3 Notes on the Asset Valuation

### Cash in hand

#### 1. Cash in hand broken down

	Total
GBP .....	41.353
EUR .....	40.865
NOK .....	26.441
SEK .....	24.730
ISK .....	22.999
USD .....	17.240
Other .....	2.438
	176.066

In January 2010 the equity injection into Arion Bank was executed, ISK 14.428 million cash (subtraction is not made in the table above), was injected to Arion Bank. Further information can be found in note 27.

#### 2. Development of cash in hand in 2009:

The increase in Cash in hand in 2009, amounting to ISK 98 billion, is driven by net proceeds from Loans to customers (principal repayments and interest payments) of ISK 88 billion, the sale of the Bank's subsidiary in Sweden of ISK 28 billion and realization of a 5.5% stake in Storebrand for ISK 20 billion. The primary outflow was due to repayments to Kaupthing Edge Germany depositors, whose claims were defined as priority claims according to Act 125/2008 of ISK 58 billion.

### Loans to and claims against credit institutions

#### 3. Loans to and claims against credit institutions specified by types of loans:

	31.12.2009			30.6.2009	31.12.2008
	Unpledged	Pledged	Total	Total	Total
Bank accounts .....	34.590	146.804	181.394	303.119	354.775
Subordinated loans to subsidiaries .....	17.983	122.982	140.965	136.150	133.528
Loans at fair value .....	-	-	-	-	29.578
Overdrafts .....	-	-	-	12	12
Other loans .....	908	-	908	3.642	4.821
<b>Loans to and claims against credit institutions .....</b>	<b>53.481</b>	<b>269.786</b>	<b>323.267</b>	<b>442.923</b>	<b>522.714</b>

The majority of unpledged bank accounts, i.e. ISK 24.530 million, are either frozen and/or have been emptied partially or fully by the counterparty without legitimate acceptable reasons being provided to the Bank. The Bank is currently attempting to retrieve these bank accounts. The largest sum is at DZ bank ISK 9.926 million and legal proceedings have commenced on that case.

The pledged bank accounts represent to a large extent collateral posted under derivative trades and repurchase agreements. Of subordinated loans to subsidiaries, the pledged position is a loan to Kaupthing Mortgage Fund. The unpledged position in this category is a subordinated bond to FIH.

#### 4. Loans to and claims against credit institutions specified by geographical location of the counterparty:

	31.12.2009			30.6.2009	31.12.2008
	Unpledged	Pledged	Total	Total	Total
Domestic .....	908	123.679	124.587	120.052	118.616
Foreign .....	52.573	146.107	198.680	322.871	404.098
<b>Loans to and claims against credit institutions .....</b>	<b>53.481</b>	<b>269.786</b>	<b>323.267</b>	<b>442.923</b>	<b>522.714</b>

### Loans to customers

#### 5. Loans to customers specified by carrying and fair value - this specification includes pledged positions:

	31.12.2009		30.6.2009		31.12.2008	
	Carrying value	Fair value	Carrying value	Fair value	Carrying value	Fair value
<b>Loans to customers .....</b>	<b>1.373.080</b>	<b>450.948</b>	<b>1.363.696</b>	<b>439.521</b>	<b>1.184.829</b>	<b>337.023</b>

Principal repayments and interest payments proceeds from the loans to customers portfolio in 2009 amounted to ISK 95 billion.

6. Loans to customers at carrying value and fair value - breakdown by portfolio:

	31.12.2009	
	Carrying value	Fair value
Europe .....	325.803	176.033
Nordic .....	231.377	152.294
NOA* .....	707.983	38.567
Pledged** .....	107.917	84.054
<b>Loans to customers</b> .....	<b>1.373.080</b>	<b>450.948</b>

\* Non-operational assets

\*\* Includes a portfolio of ISK mortgage loans, FX mortgage loans and loans to Icelandic municipalities, organisations and other government related entities, which had previously been pledged by Kaupthing Bank to the Icelandic Central Bank.

In January 2010, when the equity injection into Arion Bank was executed, ISK 28.771 million of loans from the Nordic portfolio at fair value and ISK 84.054 million of the pledged portfolio (subtraction is not made in the tables above), was injected to Arion Bank. Further information can be found in note 27.

7. Loans to customers specified by sectors:

	31.12.2009	30.6.2009	31.12.2008
	Fair value	Fair value	Fair value
Industry .....	99.980	95.463	66.280
Individuals .....	91.891	92.189	69.828
Real estate .....	83.457	74.540	55.127
Trade .....	64.129	61.363	38.967
Holding companies .....	58.715	60.674	61.283
Service .....	52.776	55.292	45.538
<b>Loans to customers</b> .....	<b>450.948</b>	<b>439.521</b>	<b>337.023</b>

Sector breakdown as at 30.06.2009 has been amended to facilitate comparison between periods since different methodology was applied in that period compared to year end figures 2008 and 2009. In the table above, the same methodology is applied across the three different periods. Hence, the numbers in this table are now directly comparable.

8. Loans to customers specified by geographical region:

	31.12.2009		30.6.2009		31.12.2008	
	Carrying value	Fair value	Carrying value	Fair value	Carrying value	Fair value
UK* .....	709.573	153.308	744.624	164.085	711.729	123.709
Scandinavia .....	228.357	152.783	246.255	143.656	168.354	88.490
Iceland .....	159.844	104.714	139.804	98.389	114.626	94.893
Other .....	275.306	40.143	233.013	33.391	190.120	29.931
<b>Loans to customers</b> .....	<b>1.373.080</b>	<b>450.948</b>	<b>1.363.696</b>	<b>439.521</b>	<b>1.184.829</b>	<b>337.023</b>

\*UK includes UK overseas territories and Crown dependencies

In almost all cases, the geographical location is determined by using the registration country.

9. Loans to customers - breakdown by currency.

	31.12.2009		30.6.2009		31.12.2008	
	Carrying value	Fair value	Carrying value	Fair value	Carrying value	Fair value
GBP .....	531.676	156.033	559.555	158.807	472.095	115.353
EUR .....	259.287	79.106	224.484	74.473	218.841	65.823
SEK .....	127.294	74.832	127.901	69.058	65.957	26.940
USD .....	234.847	40.651	237.807	35.755	238.437	35.537
ISK .....	120.899	30.837	108.078	31.285	103.099	29.953
CHF .....	39.544	30.436	37.321	26.245	29.246	24.236
JPY .....	30.040	23.367	34.230	26.076	29.342	24.497
Other .....	29.493	15.686	34.320	17.822	27.812	14.684
<b>Loans to customers</b> .....	<b>1.373.080</b>	<b>450.948</b>	<b>1.363.696</b>	<b>439.521</b>	<b>1.184.829</b>	<b>337.023</b>

10. Ten largest loans to customers - sector and country

This specification is of the fair value of loans to customers and includes pledged positions.

	31.12.2009	30.6.2009	31.12.2008
UK* / Trade .....	7,2%	7,8%	7,5%
UK* / Holding company .....	5,7%	7,8%	8,5%
UK* / Real estate .....	4,9%	4,1%	3,4%
Scandinavia / Industry .....	4,3%	4,0%	4,4%
Other / Real estate .....	4,3%	4,6%	5,0%
Iceland / Government related entity .....	3,9%	3,3%	4,0%
Scandinavia / Industry .....	3,1%	2,7%	2,7%
Scandinavia / Real estate .....	2,9%	3,2%	2,6%
UK* / Service .....	2,7%	3,1%	2,6%
Scandinavia / Industry .....	2,4%	2,0%	2,2%
<b>Ten largest loans to customers of total loans to customers .....</b>	<b>41,4%</b>	<b>42,6%</b>	<b>42,9%</b>

\* UK includes UK overseas territories and Crown dependencies

11. Loans to customers - breakdown by performance.

This specification is of the carrying value and fair value of loans to customers but does not include pledged positions.

	31.12.2009							
	Europe*		Nordic		NOA		Total	
	Carrying value	Fair value	Carrying value	Fair value	Carrying value	Fair value	Carrying value	Fair value
Performing loans .....	75,7%	96,1%	77,3%	84,3%	0,0%	0,0%	29,3%	80,2%
Loans on view list .....	0,2%	0,3%	12,3%	9,8%	0,0%	0,0%	2,4%	4,5%
Loans on watch list .....	24,1%	3,6%	10,4%	5,9%	100,0%	100,0%	68,3%	15,3%
	100,0%	100,0%	100,0%	100,0%	100,0%	100,0%	100,0%	100,0%

\* Mosaic Fashions (in administration) and the Bank's financing of NoHo Square (real-estate development at standstill) where the Bank has also all the equity are not included in the numbers presented above.

The performance categories are defined as follows:

Performing loans: Loans to entities where cash flow is sufficient to service debt, i.e. interest and principal repayments, and no breaches in agreements are foreseeable in the future.

Loans on view list: Loans to entities where cash flow is sufficient to service debt, i.e. interest and principal repayments, but agreements have been breached or are likely to be breached in the foreseeable future. Some banks include this category within performing loans.

Loans on watch list: Loans to entities where cashflow is insufficient to service debt, i.e. interest and principal repayments and agreements have been breached repeatedly.

12. Loans to customers - maturity profiles:

This specification is of the carrying value of loans to customers but does not include pledged positions.

	31.12.2009			
	Europe*	Nordic	NOA	Total
In default* .....	96.812	21.359	707.982	826.153
2010 .....	13.741	44.682	-	58.423
2011 .....	48.352	19.949	-	68.301
2012 .....	47.672	58.032	-	105.704
2013 .....	23.308	35.435	-	58.743
2014 .....	32.518	43.679	-	76.197
2015 and later .....	63.400	8.242	-	71.642
	325.803	231.378	707.982	1.265.163

Pledged positions of carrying value ISK 107.917 million is not shown in the figures above.

\* Mosaic Fashions (in administration) and the Bank's financing of NoHo Square (real-estate development at standstill) where the Bank has also all the equity are classified as being in default.

The table above is based on contractual maturity specified in the underlying loan agreements unless an acceleration event has occurred.

## Bonds and debt instruments

13. Bond and debt instruments are specified as follows:

	31.12.2009			30.6.2009	31.12.2008
	Unpledged	Pledged	Total	Total	Total
Listed .....	8.958	47.484	56.442	96.898	94.441
Unlisted .....	581	6.002	6.583	22.166	21.490
<b>Bonds and debt instruments .....</b>	<b>9.539</b>	<b>53.486</b>	<b>63.025</b>	<b>119.064</b>	<b>115.931</b>

14. Bonds and debt instruments specified by issuer:	31.12.2009			30.6.2009	31.12.2008
	Unpledged	Pledged	Total	Total	Total
Financial institutions .....	-	33.853	33.853	43.765	41.428
Housing Financing Fund .....	4.656	8.828	13.484	46.146	45.807
Government .....	4.302	8.637	12.939	24.687	24.682
Corporates .....	581	2.168	2.749	4.466	4.014
<b>Bonds and debt instruments .....</b>	<b>9.539</b>	<b>53.486</b>	<b>63.025</b>	<b>119.064</b>	<b>115.931</b>

The decrease from 30 June 2009 to 31 December 2009 in pledged positions is driven by the settlements of collateralized agreements. In addition, the pledged positions are now represented at the assumed market value of the underlying collateral as at the Bank's interpretation of the valuation date of the underlying agreements.

## Shares and instruments with variable income

15. Shares and instruments with variable income are specified as follows:

	31.12.2009			30.6.2009	31.12.2008
	Unpledged	Pledged	Total	Total	Total
Listed .....	5.118	149.530	154.648	199.619	153.274
Unlisted .....	23.731	-	23.731	14.981	8.577
<b>Shares and instruments with variable income .....</b>	<b>28.849</b>	<b>149.530</b>	<b>178.379</b>	<b>214.600</b>	<b>161.851</b>

16. Ten largest positions:

	31.12.2009			30.6.2009	31.12.2008
	Unpledged	Pledged	Total	Total	Total
Trade/UK .....	-	43.474	43.474	51.246	45.191
Service/UK .....	-	33.769	33.769	48.489	26.285
Financial/Scandinavia .....	-	29.835	29.835	30.462	28.351
Industry/UK .....	-	24.246	24.246	23.470	15.403
Financial/Scandinavia .....	-	7.022	7.022	26.720	21.364
Industry/Other .....	6.671	-	6.671	4.130	2.015
Industry/Iceland .....	-	6.001	6.001	6.174	6.174
Retail/UK .....	5.674	-	5.674	-	-
Service/Scandinavia .....	180	4.879	5.059	7.486	7.486
Financial/Other .....	4.494	-	4.494	3.939	3.047
<b>Ten largest positions total .....</b>	<b>17.019</b>	<b>149.226</b>	<b>166.245</b>	<b>202.116</b>	<b>155.316</b>

The pledged positions are now represented at the assumed market value of the underlying collateral as at the bank's interpretation of the valuation date of the underlying agreements.

## Derivatives and unpaid derivatives - assets

17. Derivatives and unpaid derivatives are specified as follows by status:

	31.12.2009		30.6.2009		31.12.2008
	Carrying value	Provision	Fair value	Fair value	Fair value
Derivatives .....	18.265	(10.684)	7.581	24.417	43.098
Unpaid derivatives* .....	372.964	(141.528)	231.436	221.656	190.764
<b>Derivatives and unpaid derivatives .....</b>	<b>391.229</b>	<b>(152.212)</b>	<b>239.017</b>	<b>246.073</b>	<b>233.862</b>

Estimated netting effects on derivatives on the asset side amount to ISK 120.204 million.

\* Matured and terminated trades, and unpaid cash flow from open trades

18. Derivatives and unpaid derivatives are specified as follows by type:

	31.12.2009		30.6.2009		31.12.2008
	Carrying value	Provision	Fair value	Fair value	Fair value
Unpaid FX Trades, Asset Swaps, Interest Rate Swaps, FX Options* ..	372.245	(140.793)	231.452	220.320	189.493
Open FX Trades, Asset Swaps & Interest Rate Swaps .....	16.275	(8.962)	7.313	23.264	42.651
Unpaid Credit Derivatives* .....	(5.935)	(43)	(5.978)	(2.828)	(2.693)
Unpaid Equity Options* .....	6.491	(589)	5.902	3.638	3.463
Open Caps, Floors, Barriers .....	1.991	(1.722)	269	1.153	447
Unpaid Caps, Floors, Barriers* .....	162	(103)	59	526	501
<b>Derivatives and unpaid derivatives .....</b>	<b>391.229</b>	<b>(152.212)</b>	<b>239.017</b>	<b>246.073</b>	<b>233.862</b>

A derivative contract is accounted for as an asset if the total net position of all derivatives contract of the counterparty is in the bank's favour. Negative unpaid carrying value in the analysis of assets is therefore always counteracted by positive values of other contracts by the same counterparty.

Estimated netting effects on derivatives on the asset side amount to ISK 120.204 million.

\* Matured and terminated trades, and unpaid cash flow from open trades

## Investments in subsidiaries

19. Investments in subsidiaries at 31 December 2009 are specified as follows:

	Functional currency	Ownership	31.12.2009		30.6.2009	31.12.2008
			Pledged	Total	Total	Total
FIH Erhvervsbank, Denmark .....	DKK	99,9%	97.047	97.047	91.168	86.213
Kaupthing Mortgage Inst. Investor Fund, Iceland .....	ISK	100,0%	17.303	17.303	18.317	17.544
Norvestia Oyj, Finland .....	EUR	32,7%	-	8.776	8.139	7.445
NBS Diversified Credit Fund, UK .....	EUR	100,0%	-	6.264	5.898	5.898
Kaupthing Sverige AB, Sweden .....	SEK	100,0%	-	5.103	5.734	5.403
Kirna ehf., Iceland .....	ISK	100,0%	-	3.557	5.375	5.375
Other .....	-	-	-	3.576	931	1.586
<b>Investments in subsidiaries .....</b>			<b>114.350</b>	<b>141.626</b>	<b>135.562</b>	<b>129.464</b>

The equity stake in FIH Erhvervsbank is shown as fully pledged against a liability at the Icelandic Central Bank.

The Bank controls 56.0% of the votes in Norvestia Oyj despite holding only 32.7% of outstanding shares, and the company is thus considered to be a subsidiary of the Bank.

## Other assets

20. Other assets are specified as follows:

	31.12.2009	30.6.2009	31.12.2008
	Total	Total	Total
Accounts receivables .....	40.549	37.887	35.513
Sundry assets .....	4.003	6.429	10.293
Provisions .....	(37.012)	(35.214)	(32.445)
<b>Other assets .....</b>	<b>7.540</b>	<b>9.102</b>	<b>13.361</b>

## Other Information

### Liabilities to Arion Bank hf. in return of assets and liabilities transferred

21. In October 2008 all of the Bank's deposit liabilities in Iceland were transferred to Arion Bank (previously New Kaupthing), and also the bulk of the Bank's assets that relate to its Icelandic operations, such as loans and other claims. This transfer was done according to the FME's Transfer Decision dated 21 October 2008. Negotiations on the valuation of the assets and liabilities were concluded on 3 September 2009 when the Government and the Bank agreed not to conclude the valuation of the assets at present but in 3 years time. This solution allows the Bank to capture further upside in the valuation of the assets.

The Bank is to provide cover for any negative initial value ("valuation gap") from the transfer of assets and liabilities from the Bank to Arion Bank; the valuation gap is assessed at ISK 38.358 million as at 22 October 2008. The value of the assets is guaranteed for the time period of the agreement which ends 30 June 2012. The valuation gap amounted to ISK 44.927 billion as at 31 December 2009. The valuation gap is denominated 50% in EUR and 50% in ISK. The current increase in the valuation gap is due to currency movements and accrued interests. The size of the valuation gap will be reassessed annually by an independent auditor - the first reassessment will be made in April 2010. Therefore, the size of the valuation gap can decrease but has been capped at the initial value save for currency movements and accrued interests.

### Claims for administration of the estate and known priority claims

22. Claims for administration of the estate and known priority claims are specified as follows:

	31.12.2009	30.6.2009	31.12.2008
Liability to Arion Bank in return of assets and liabilities transferred .....	44.927	43.335	41.027
Liability to Arion Bank .....	-	7.547	9.123
Accounts payable - costs of managing the Bank while in moratorium process .....	612	-	-
Deposits .....	6	2.140	54.775
Liability to Norway and Finland regarding deposits .....	-	-	14.130
<b>Known claims for administration of the estate and known priority claims .....</b>	<b>45.545</b>	<b>53.022</b>	<b>119.055</b>

The table above is put forth for illustrative purposes only and represents claims for administration of the estate and priority claims that are known to the ResCom. Until all claims have been recognized and disputes settled by the Winding-up Committee, the real and accurate amount of liabilities, including but not limited to priority claims, is uncertain. It should also be noted that this table is put forth by the ResCom and does not reflect the decisions of the Winding-up Committee on individual claims.

23. Total assets net of pledged assets and known priority claims\* - netting due to derivatives taken into account:

	31.12.2009	Pledged positions	Known priority claims*	31.12.2009 Estimated valuation	30.6.2009 Estimated valuation	31.12.2008 Estimated valuation
<b>Assets</b>	<b>Total assets</b>					
Cash in hand .....	176.066	-	-	176.066	98.799	77.963
Loans to and claims against credit institutions .....	323.267	(269.786)	-	53.481	42.899	148.548
Loans to customers .....	450.948	(84.054)	-	366.894	357.259	259.666
Bonds and debt instruments .....	63.025	(53.486)	-	9.539	12.344	2.652
Shares and instruments with variable income .....	178.379	(149.530)	-	28.849	35.055	23.203
Derivatives and unpaid derivatives .....	239.017	(120.204)	-	118.813	102.556	96.626
Investments in subsidiaries .....	141.626	(114.350)	-	27.276	26.077	25.707
Other assets .....	7.540	-	-	7.540	9.102	13.361
<b>Total assets .....</b>	<b>1.579.868</b>	<b>(791.410)</b>	<b>-</b>	<b>788.458</b>	<b>684.091</b>	<b>647.726</b>
Claims for estate admin and known priority claims .....	-	-	(45.545)	(45.545)	(53.022)	(119.055)
<b>Total assets after subtracting .....</b>	<b>1.579.868</b>	<b>(791.410)</b>	<b>(45.545)</b>	<b>742.913</b>	<b>631.069</b>	<b>528.671</b>

\* Claims for administration of the estate and known priority claims represent liabilities which are listed by the ResCom in note 22. Until all claims have been recognized and disputes settled by the Winding-up Committee, the real and accurate amount of liabilities, including but not limited to priority claims, is uncertain. It should also be noted that this estimate is put forth by the ResCom and does not reflect the decisions of the Winding-up Committee on individual claims.

The valuation herein of the Bank's assets is based on the methodologies described in chapter 2.1.1 Valuation Methodology and is a historical valuation only. No attempts were made at this time to assess the possible future value of assets, nor to estimate likely recovery of creditors' claims.

Contrary to prior accounts published by the ResCom, derivatives and collateral posted against derivatives are shown on a netted basis. Comparison numbers from past periods have been amended on approximate basis to reflect this as well to facilitate comparison to past periods.

The table above does not fully take into account the impact of set-off as further described in note 24.

It should also be noted that there were significant movements in foreign exchange rates in 2009.

#### 24. Set-off

The valuation of assets and liabilities in this report does not take fully into account the impact of set-off.

The real and accurate amount of set-off claims accepted remains uncertain until recognized and disputes settled by the Winding-up Committee. The Winding-up Committee received set-off claims from close to 100 counterparties amounting to approximately ISK 650 billion. It should be noted that set-off claims are lodged in different ways and many of them are lodged at a maximum level. Not all claims regarding set-off may fulfill the conditions that a declaration for set-off must fulfill according to Icelandic law and in some cases creditors only reserve the rights to a possible set-off. All amounts regarding set-off must be reviewed bearing that in mind.

As at 20 October 2009, the Resolution Committee put forth preliminary estimated set-off effects where it estimated that in total up to ISK 100 billion on the face value of both the respective assets and the respective liabilities could be subject to set-off. The committee also noted that the set-off effects on the assets and liabilities side may differ. The list of set-off claims increased substantially in the latter half of the claim filing period which ended 30 December 2009 and at that time, the list of set-off claims amounted to ISK 650 billion. The Resolution Committee has independently reviewed the list of set-off claims provided by the Winding-up Committee on an approximate and rough basis. The Resolution Committee's conclusion after the revision of the list is to revise its current estimation on set-off effects to ISK 100 - 150 billion in total on the face value of the respective liabilities. As the Resolution Committee has noted before, the exact set-off effects on the assets and liabilities side may differ and the committee estimates that the effects on the asset side will be substantially lower since some of the assets that are subject to set-off have already been impaired or provisioned for. The committee's estimation takes into account the fact that substantial amount of the set-off claims filed are already accounted for in note 23. It should also be stressed that this estimation is put forth by the Resolution Committee and does not reflect the decisions of the Winding-up Committee on individual claims.

Set-off impacts can make a material difference to overall creditor recoveries. Further information will be provided on this matter as it becomes available.

#### 25. Claim process

A formal process for the creditors of the Bank to file claims against the Bank began on 30 June 2009 and ended on 30 December 2009. Until the Winding-up Committee has recognized all claims and disputes have been settled, the real and accurate amount of liabilities is uncertain. According to Act no. 44/2009, all claims should have been filed as at 22 April 2009 in the relevant currency and converted into ISK at the exchange rate published by the Central Bank of Iceland on 22 April 2009.

The estimated liability side fixed as at 22 April 2009 was published in the Bank's half year accounts as at 30 June 2009. The claim registry was published by the Winding-up Committee as at 22 January 2009. In note 26, the ResCom has roughly categorized the claim registry in order for it to be comparable with the previously published liability side of the balance sheet as at 30 June 2009. Revision of claims which had been fixed as at 22 April 2009 was not carried out since the responsibility of determining the liability side of the balance sheet is placed with the Winding-up Committee through a strict legal process set out in Act no. 161/2002 on Financial Undertakings and Act no. 21/1991 on Bankruptcy etc.

The liabilities of the Bank are currently being determined through a formal claims filing process which is administered by the Winding-up Committee of the Bank. The scope of the liabilities of the Bank remains uncertain until the legal process of recognizing and rejecting claims has been further progressed by the Winding-up Committee. In the event there are discrepancies between the liabilities estimate presented by the Resolution Committee and the claims against the Bank as finally determined by the Winding-up Committee, the determination of liabilities by the Winding-up Committee prevails.

In total of 28,085 claims were lodged against Kaupthing Bank by the deadline for lodging claims on 30 December 2009. Claims against the Bank were received from creditors in 119 countries, over half of them interest claims from Germany, mostly related to deposits. Among the largest creditors are domestic parties, domestic and foreign financial institutions, and various investment funds abroad, including venture capital funds, mutual funds and hedge funds.

The total amount of claims lodged is ISK 7,288 billion, at the ISK exchange rates of the Central Bank of Iceland on 22 April 2009. The aggregate amount of claims exceeds the Bank's liabilities as recognized in its balance sheet of 30 June 2009. The difference can in part be explained by claims lodged for deposits which the Bank has already repaid, significant amount of bond claims and some deposits claims lodged in duplicate or triplicate, off-balance sheet items, such as claims for damages and guarantees. Furthermore, creditors generally lodge claims at maximum levels. The aforementioned claims add up to at least ISK 2,900 billion.

As at 29 January 2010, the Winding-up Committee had made decisions on over 16,000 claims or approx. 57% of the total number of claims lodged. By far the greatest numbers of those were for interest on deposits from Germany, which were received in a fairly steady stream throughout the claims period. Most claims from banks and financial undertakings, on the other hand, were received near the end of the deadline. Following the creditors' meeting of 29 January, the Winding-up Committee has continued to take decisions on those claims lodged for which decisions have not been taken. A follow-up creditors' meeting will be held on 18 May 2010 where the Winding-up Committee will present its decisions on claims on which decisions have not been taken prior to the meeting on 29 January 2010, in so far as possible. At that meeting the Winding-up Committee intends to have completed its decisions on all claims lodged on the basis of Articles 109, 110, 111 and 112 of the Act on Bankruptcy etc., No. 21/1991. Work will proceed in tandem to this on decision on bond claims and other unsecured claims.

26. Comparison of liabilities between claim registry and the Bank's balance sheet as at 30.06.2009:

	30.6.2009 Balance sheet	Claim registry			
		Total Claims	Priority	General	Subordi- nated
Due to credit institutions .....	151.808	-	-	-	-
Deposits .....	2.140	58.588	21.779	35.688	1.121
Derivatives and unpaid derivatives .....	136.296	502.965	48.403	435.697	18.865
Borrowings .....	3.237.006	-	-	-	-
Bonds .....	-	3.431.151	133.719	3.119.568	177.864
Loans .....	-	570.084	205.566	358.898	5.620
Deposit agreements .....	-	297.791	204.809	89.389	3.593
Liability to Arion Banki in return of assets and liabilities transferred .....	43.335	43.568	43.568	-	-
Other liabilities .....	108.302	-	-	-	-
Invoices .....		4.114	1.241	2.616	257
Edge interest claims .....		6.130	5.347	692	92
Guarantees .....		1.098.334	964.808	132.167	1.358
Damage claims .....		645.424	459.060	119.841	66.524
Contracts .....		51.120	1	51.118	
Reimbursements .....		1.632	1.308	315	9
Miscellaneous .....		176.948	20.707	156.215	26
<b>Total senior liabilities</b>	<b>3.678.887</b>	<b>6.887.848</b>	<b>2.110.316</b>	<b>4.502.203</b>	<b>275.329</b>
Subordinated loans .....	422.624	400.802	862	291.373	108.567
Interest expense from 22.4.2009-30.06.2009 .....	27.804				
<b>Total subordinated liabilities</b>	<b>450.428</b>	<b>400.802</b>	<b>862</b>	<b>291.373</b>	<b>108.567</b>
<b>Total liabilities</b>	<b>4.129.315</b>	<b>7.288.650</b>	<b>2.111.178</b>	<b>4.793.576</b>	<b>383.896</b>

This table above is put forth for illustrative purposes only. The claim registry is based on numbers provided by the Winding-up Committee which have not been reviewed by the ResCom. Detailed matching between the claim registry and the balance sheet has not been completed and hence, claims in each bucket of the liability side of the balance sheet may not be directly comparable to the claim registry.

It should also be noted that amounts according to claim registry are put forth for information purposes only and do not reflect the decisions of the Winding-up Committee on individual claims.

Some disparity may be between number of claims and amounts according to claim registry as shown above and the number of claims and amounts in the claim registry made available to creditors by the Winding-Up Committee on 22 January 2010. This is due to the fact that the Winding-up Committee has made numerous corrections on the claim registry, both with regards to number of claims and amounts. Several claims have also been withdrawn. An updated claim registry along with corrections of list of claims is available for creditors at a secure site on [www.kaupthing.com](http://www.kaupthing.com)

**Events occurring after 31 December 2009**

27. Investments in subsidiaries - explanation of the equity injection into Arion Bank and the effects on the balance sheet.

On 11 January 2010 the Icelandic Financial Authority (FME) granted Kaupthing Bank's subsidiary Kaupskil ehf. permission to own a qualifying holding in Arion Bank on behalf of Kaupthing. This permission was given following the conclusion of an agreement on the ownership of Arion Bank between Kaupthing Bank and the Ministry of finance.

Kaupthing, through its subsidiary Kaupskil ehf., contributed assets valued as at 8 January 2010 at ISK 66.000 million equivalent to 65% of the overall capitalization of Arion Banki for which it received 87% of the share capital. Kaupthing capitalised Arion Bank in the following manner.

	Carrying value	Market value
Corporate Loans .....	29.424	28.771
Other loans * .....	107.917	84.054
Cash .....	14.428	14.428
Liability to the Icelandic Central Bank .....	(61.253)	(61.253)
<b>Equity injection into Arion bank</b> .....	<b>90.516</b>	<b>66.000</b>

\* a portfolio categorized under Loans to customers under the name Pledged and consists of ISK mortgage loans, FX mortgage loans and loans to Icelandic municipalities, organisations and other government related entities, which had previously been pledged by Kaupthing Bank to the Icelandic Central Bank valued at ISK 84.054 million (net ISK 22.802 million after the corresponding liability of ISK 61.253 million towards the Icelandic Central Bank has been transferred to Arion Bank).

The assets were evaluated at the transfer price to Arion Bank. The effects on the balance sheet of Kaupthing Bank will be that these assets will be deducted from the relevant asset classes and the total, ISK 66.000 million is booked under Investments in subsidiaries.

#### Foreign exchange rates

The foreign exchange rates used in the preparation of this financial information as at 31 December 2009 is based on Reuters foreign exchange rates as at 16:30 on that date. The table below displays the foreign exchange rates used for the balance sheet as at 31 December 2009 and the foreign exchange rates for past comparison periods.

	<u>31.12.2009</u>	<u>30.6.2009</u>	<u>31.12.2008</u>
AUD .....	112,53	102,90	84,46
CAD .....	119,74	109,91	98,72
CHF .....	121,18	117,78	113,82
DKK .....	24,16	24,04	22,73
EUR .....	179,78	179,04	169,27
GBP .....	202,65	210,04	176,48
JPY .....	1,35	1,32	1,34
NOK .....	21,63	19,84	17,39
SEK .....	17,54	16,52	15,44
USD .....	125,43	127,56	121,10

## 2.2 The Loan Portfolio

### 2.2.1 Overview

Loans to customers are divided into four portfolios:

- **Nordic portfolio:** the vast majority of loans to customers in the Nordic region.
- **Europe portfolio:** the vast majority of loans to customers in Europe.
- **NOA portfolio:** mainly non-operating assets.
- **Pledged:** Includes a portfolio of ISK mortgage loans, FX mortgage loans and loans to Icelandic municipalities, organisations and other government related entities, which had previously been pledged by the Bank to the ICB. In January 2010, when the equity injection into Arion Bank was executed, the assets of this pledged portfolio was injected to Arion Bank.

The Nordic and Europe portfolios are actively managed by the asset management team and the vast majority of the stakes in these portfolios have underlying operations or assets.

The loans in the NOA portfolio are under the supervision and management of the Inspection Committee and undergo thorough revision by the Committee.

Loans to customers at nominal value amounted to ISK 1.373bn as at 31 December 2009.

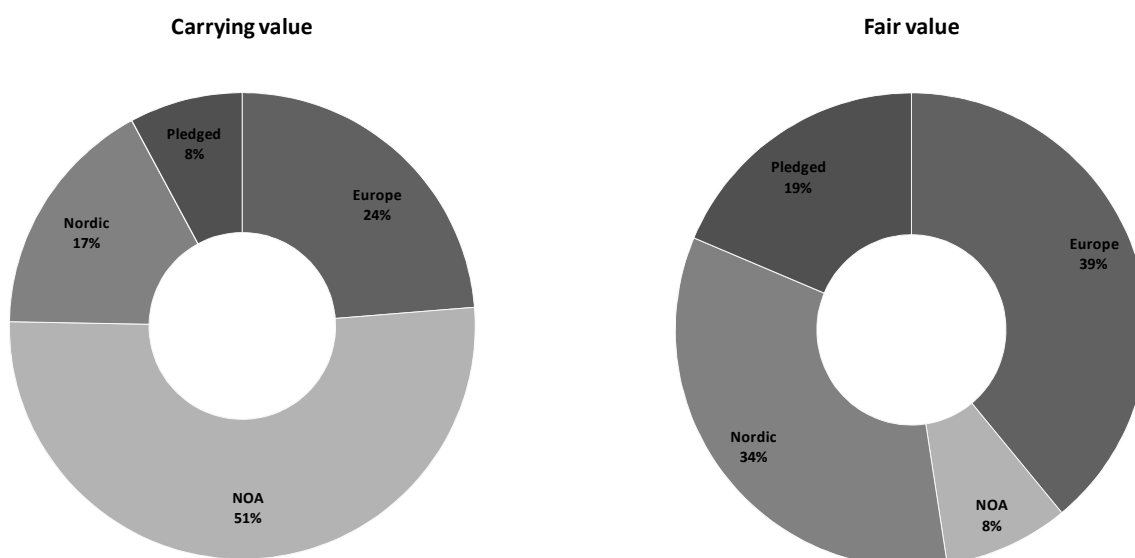
Loans to customers at fair value amounted to ISK 451bn as at 31 December 2009.

Fair value of *Loans to customers* as at 31 December 2009:

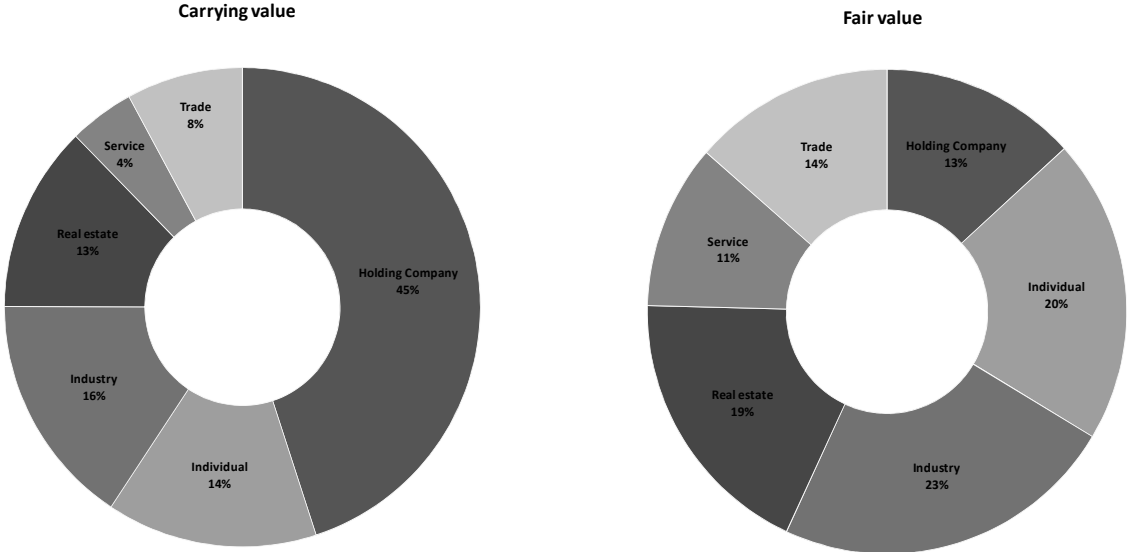
- **Nordic portfolio:** approx. ISK 152bn
- **Europe portfolio:** approx. ISK 176bn
- **NOA portfolio:** approx. ISK 39bn
- **Pledged:** approx. ISK 84bn

Further breakdown of the portfolios are shown below.

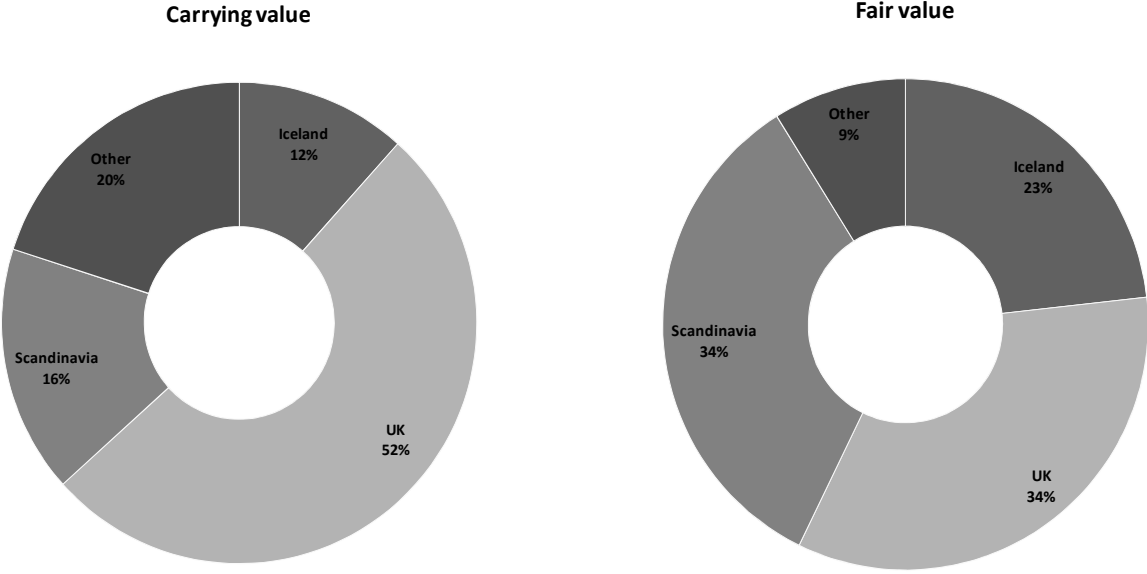
Loans to customers broken down by portfolios as at 31 December 2009:



Loans to customers broken down by sector as at 31 December 2009:

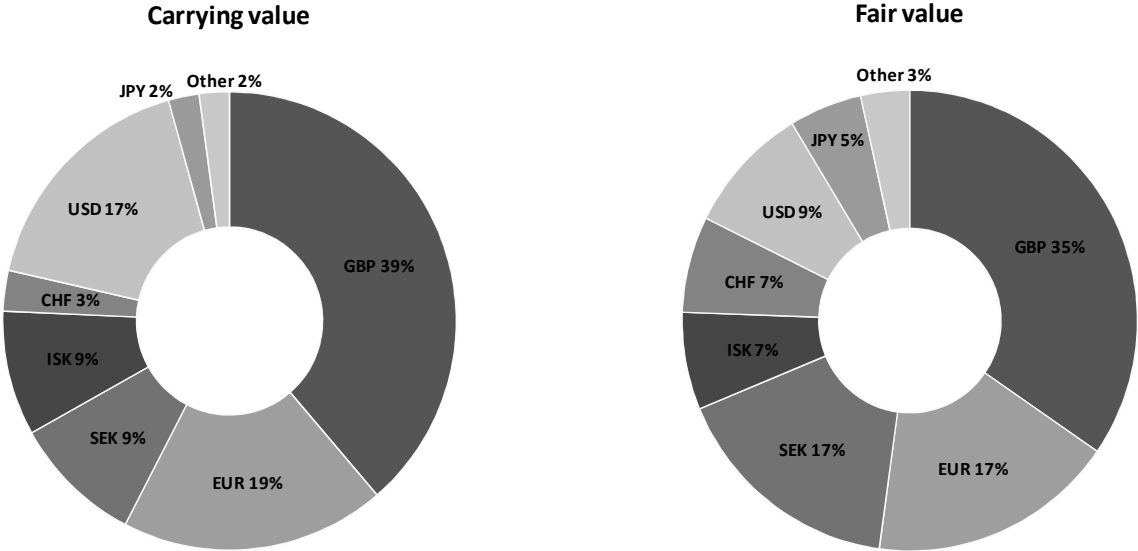


Loans to customers broken down by geography as at 31 December 2009:



\*UK includes UK overseas territories and Crown dependencies

Loans to customers broken down by currency as at 31 December 2009:



### 2.2.2 Loans under AM

As mentioned before, the Nordic and Europe portfolios are actively managed by the asset management team and the vast majority of the stakes in these portfolios have underlying operations or assets.

The mandate of the asset management division can be divided into five steps: stabilization, consolidation, full overview, which leads to the ordinary management of the loans and ends with an exit strategy.

*Stabilization:* The Asset Management team was up against major challenges in the beginning. The main task was to stabilize the situation and to retain value wherever possible by preventing the collapse of different assets and by refusing strongly any fire sale bids.

*Consolidation:* The Bank protected assets in its foreign entities in the Nordic region and finally managed to transfer assets back to the parent company. Loans were transferred from branches and a subsidiary in the Nordic region to the parent company.

*Full overview:* Once the initial challenges had been overcome, a more comprehensive and thorough approach was taken on the loan portfolio. Responsibility was allocated between employees from asset management, portfolio management, finance and legal counsel. Loans were analyzed and prioritized by urgency and size. A detailed facility by facility review was carried out and strategies for all exposures and their recovery have been formulated.

*Management:* With a full overview of the loan positions, the Bank went into ordinary management and relevant actions were taken for each asset. The aim is to secure maximum recovery with pro-active management of the loans. Further objectives for each loan are set and, when appropriate, external advisors and consultants are hired to ensure top class expertise.

*Exit strategy:* When previous steps have been completed a solid foundation has been set up for the development of a medium to long term strategy for each loan with the aim of ensuring realization of its maximum value. The loans are developed into more stable and sellable form. The work has been focused on value creation, keeping in mind the eventual realization of value, but to date the focus has not been on the formalization of exit strategies and very few loans have been sold.

The ultimate goal is to develop the optimal solution for each loan and thereby maximize recovery value for the creditors of the Bank.

### 2.2.3 NOA portfolio

The Non Operating Assets portfolio ("NOA") is under the supervision of a sub-committee of the ResCom, the Inspection Committee ("IC") and comprises of loans, securities and transactions under examination. IC is responsible for maximizing recovery of assets in the portfolio. The primary aspects of its work are: reviewing and investigating these transactions, and to prepare and commence legal proceedings and collection against parties that might be liable to the Bank as a result of those transactions. The matters in the portfolio that the IC is reviewing with a view to recovery and claims consist of: loans to related parties, irregular loans or transactions, loans and transactions related to subsidiaries and other matters which have been directed to the IC.

All decisions on matters related to the NOA portfolio are made by the IC. The committee comprises two people, both of whom are members of the ResCom. Two internal dedicated teams are working for the committee. Each team comprises an account manager and a lawyer. These teams are responsible for managing the matters within the NOA portfolio on a day-by-day basis with the support of various internal departments and staff. The committee primarily works with two external advisors, such as forensic auditor Grant Thornton UK and the international law firm Weil, Gotshal & Manges UK.

From October 2008 and throughout 2009, the IC's work has been based on the same principles as the Asset Management division, which has been to stabilise the portfolio, acquiring overview of each asset and taking actions where necessary to secure the assets and maximise recovery.

Approx. 85% of the portfolio is holding companies and other SPV's which are mainly non-domestic entities. The portfolio currently comprises more than 20 structures which are under examination. They are all categorised as being under watch until the Inspection committee has concluded its examination. The number of entities in each structure under examination ranges from 1 to more than 250. Loans and historical transactions in this portfolio are scrutinized where dealings and documents for each borrower are thoroughly examined.

In autumn 2008, the ResCom, at the request of the FME, engaged PwC to investigate whether the Bank or parties connected to it, had in the weeks before the collapse of the bank deviated from its internal rules or violated the rules governing the activities of financial undertakings, the securities transactions act or the general penal code. A detailed report was submitted to the FME on 30 December 2008 and it has already become the basis for further investigations.

External legal counsel is currently working with the IC and the internal teams, along with forensic accountants, on examining 11 structures. Majority of the loans in the portfolio are in default. Legal collection proceedings and/or enforcement actions have been commenced against entities in 11 of the structures. The committee has been successful in securing the assets and prevent leakage of assets from various structures through enforcing pledges and bringing legal actions (for example court procedures and commencing insolvency procedures). The committee has obtained repayments (whether full or partial) from a number of entities under examination and has also taken control of some assets through the enforcement of pledges. In addition, one company recovered through legal action has been transferred to the Asset Management division for active management. The committee has at the same time reported incidents of possible misconduct to various regulators and investigation bodies. Such incidents are also being reviewed by the Inspection Committee for potential damages claims where such claims may maximise the assets of the bank.

The Winding-up Committee has engaged PwC Iceland to investigate measures taken by the Bank before it was granted a moratorium and the IC will be working closely with the Winding-up Committee and PwC Iceland who are focussing particularly on possible rescissions and damages claims in relation to domestic parties.

For the year 2010 and onwards, the main objective of the IC is to continue to focus on the maximisation of the recovery of assets in the portfolio, including by bringing damages claims where appropriate. Having exercised security over the majority of liquid assets secured, the IC intends to finalise the exercise of security over the remaining assets. Receiverships and liquidations which have been commenced or are about to commence will continue in order to realise assets in the companies under receivership and also to access information which will enable the IC to investigate additional potential claims for recovery. The IC also intends to continue or commence legal proceedings for recovery and damages claims as and when sufficient information and evidence can be collected and the potential recovery under such claims can be properly analysed.

#### **2.2.4 Restructuring**

The objective of all restructuring efforts is to maximize the likelihood of recouping the Bank's previous full exposure, protecting the Bank's interests and the company value going forward. Before restructuring the account is analyzed extensively, taking into account various other options, other creditors, collateral position etc.

Common scenarios where restructuring is a real option:

- Insufficient cash flow to service the debt, the company has no real equity and there is a risk of management behaving irrationally.
- Potential equity value and the Bank gains a legal avenue to the asset due to e.g. covenant breaches.

Following are important practicalities which the Bank takes into account when executing a capital restructuring. The aim is to find the right balance between:

- Operational disruptions and the possible outcome of the restructuring exercise.
- The costs associated with the financial restructuring and its complications, against future cost savings while bearing in mind how easily the structure can be managed.
- What incentives to give to other stakeholders: sound understanding of the company’s future prospects and its value are of utmost importance in this respect.

The aim is to set the debt level not lower than perceived enterprise value at restructuring.

**Progress in restructuring work**

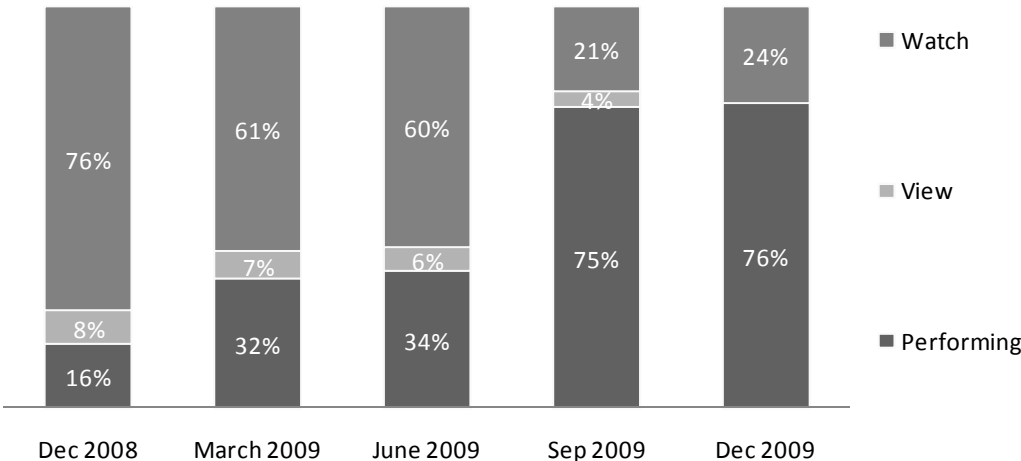
In December 2008, 76% of Europe portfolio and 41% of the Nordic portfolio (since March 2009) was on the Bank’s watch list (or had the risk of getting there). Those are loans whereby cash flow is insufficient to service debt and there are (repeated) covenant breaches. Some of which (a) are in industries badly hit by recession; or (b) had owners that were distressed because of the financial crises and unable to support their assets; or (c) had the wrong capital structure to start with.

Considerable part of the Nordic and Europe loan portfolio have undergone restructuring in 2009. At the year-end 2009, only approx. 24% of the Europe and 11% of the Nordic loan balance were still on the watch list. The status of loan portfolios is categorised in the following manner:

- *Performing loans*: Loans to entities where cash flow is sufficient to service debt, i.e. interest and principal repayments and no breaches in agreements are foreseeable in the future.
- *Loans on view list*: Loans to entities where cash flow is sufficient to service debt, i.e. interest and principal repayments, but agreements have been breached or are likely to be breached in the foreseeable future. Some banks include this category within performing loans.
- *Loans on watch list*: Loans to entities where cash flow is insufficient to service debt, i.e. interest and principal repayments and agreements have been breached repeatedly.

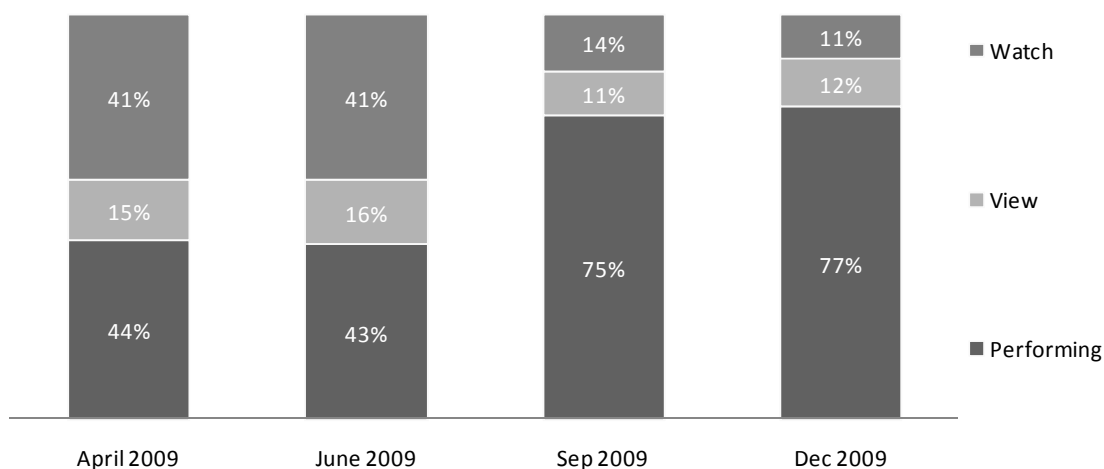
The graphs below shows the portfolios based on the nominal value in the respective month.

**Europe portfolio\***



\*The Europe portfolio excludes post restructuring debt which is still on Mosaic Fashions (in administration) and the Bank’s financing of NoHo Square (real-estate development at standstill) where the Bank has also all the equity.

## Nordic portfolio



Majority of the loans in the Nordic portfolio were transferred from the respective countries in Q1 2009.

This increase is to a large extent the result of extensive financial restructuring and covenant resets.

The Bank has acquired a controlling interest in several companies and the Bank has, as an equity holder, made sure that its views are presented by nominating board members while also making sure to retain other board members with industrial know-how and expertise. The Bank has already started to see equity value being created in some of the restructuring cases, however, the book value of those equity stakes was at zero in the Bank's balance sheet as at 30 June 2009.

In all of the major restructuring cases, the Bank has hired external advisors. Depending on the nature of the restructuring projects, these external parties can be financial advisors, legal counsels, real estate consultants, retail experts, accountants, auditors in the relevant countries etc. The cost of these is in most cases paid by the respective borrower.

### **Restructuring – case studies**

Following is list of some restructuring cases implemented by the Bank. This list cannot be taken as conclusive.

#### *Aurora Fashions / Mosaic Fashions*

The Bank and the former senior management of Mosaic Fashions established Aurora Fashions Limited ("Aurora") to take over the retail brands Karen Millen, Coast, Warehouse and Oasis, which previously belonged to Mosaic Fashions Limited ("Mosaic"). The administrators which were appointed to Mosaic Fashions sold in an asset deal parts of Shoe Studio to Dune and parts of the Principles assets to Debenhams. This operation was completed with considerable efforts from Deloitte, DLA Piper and BDO Stoy Hayward.

Mosaic had been experiencing significantly deteriorating earnings due to the UK recession compounded by financial difficulties. After attempts to restructure the business in consultation with key stakeholders, Mosaic's board of directors decided on 1 March 2009 to request that the company be put into administration. This step was necessary as it seemed clear that Mosaic would not be able to meet its obligations to its creditors. Furthermore, attempts to restructure the business with a view to securing its continued operations had failed.

Currently, Aurora is financially sound with reduced capital requirements and fit to meet the challenges in the retail market. The new structure will strengthen the brands by bringing a greater management

focus to operations and providing opportunities to create a more flexible cost structure by reducing fixed expenses.

To date the transaction has proved successful although the UK retail environment still remains challenging. The aim is to continue focusing on de-leveraging the business but also preserving the upside if and when the retail market recovers. Once the benefits of Aurora's strategy become evident, the ResCom is confident that there will be a significant recovery for the Bank.

#### *All Saints*

To project the Bank's exposure to a shareholder loan, the Bank reached an agreement with the main shareholders of the British retail chain All Saints, which will consolidate the company's position as the leading design led brand on the British market. All Saints was founded in 1994 and was acquired by Kevin Stanford in 2003, at which point its sales were less than GBP 5m. Since then the company has been transformed into a brand that holds a strong position on the British High Street. The company has demonstrated robust growth in both revenues and strong LFL performance in challenging market conditions. The Bank rates the company's prospects positive going forward despite the difficult conditions in the UK retail market. Furthermore, this enabled the company to secure GBP 30m refinancing of its debt and further grow its business in the UK and internationally. These agreements removed the uncertainty over the company's shareholding and funding, and allow it to continue its growth.

#### *Former Middlesex Hospital Site*

The Bank has commenced a sales process for the Middlesex Hospital Site in core of West End in London. Following a detailed strategy review, the Bank engaged CB Richard Ellis on the sale of the former Middlesex Hospital site.

The Bank has been working with UK developer Stanhope to identify different options for the three acre West End site over the last eight months. In light of the strong market recovery and a number of approaches, the Bank decided to put the site into a formal sales process.

The Middlesex Hospital site has a MAKE designed consented scheme for a 900,000 sq ft residential and office mixed use redevelopment.

#### *Huurre Group Oy*

The Bank supported a major restructuring of one of North-Europe's leading commercial refrigeration companies, Huurre Group Oy (HQ in Finland) to strengthen the Group's financial position in the current challenging economical climate. As a result of this, the equity ratio of the Group has been substantially improved. Simultaneously, the loan facilities have been extended, having now a maturity of three years securing the Group's financing to mid 2012. Following the restructuring, the Bank now owns 100% of the Group's equity. For the restructuring, PwC participated in the valuation and regarding business sensitivity study. Deloitte advised on tax and structuring and Olswang and Borenus gave advice on legal issues and documentation.

#### *Bay Restaurant Holdings Limited and Town & City Pub Company Limited*

Plato Company 3 Ltd, is the 100% holding company of Bay Restaurant Group Limited and Town & City Pub Company Limited. The combined group was highly leveraged and the Bank owned a substantial part of its debts or close to 60%. The rest of the debt was owned by a single bank. The group agreed with its banks, on a partial debt-for-equity swap conversion which has reduced its debt by approx. GBP 90m. The capital restructuring has enabled the two operating companies to focus on its operations in tough market conditions. The restructuring resulted in the Bank becoming a major shareholder of the combined group. Both companies have done well in this fiscal year and are outperforming budget. For this transaction, PwC gave advice on tax and restructuring and Slaughters & May on legal issues and documentation.

#### *PMS properties*

The Bank has finished the restructuring of a SEK 1,1bn portfolio of twelve properties in Sweden. Eleven out of the twelve properties were refinanced in cooperation with the previous owners, the P.M.S. Group Ltd. in Israel, while one of the assets was refinanced through a bankruptcy process. A proactive approach taken by the Bank has secured a considerable equity injection by the owners in both processes and a profit sharing structure. The loans mature in less than five years time and include prepayment incentives for the borrowers.

### *Celsius portfolio*

The Bank has agreed with the shareholders of the Celsius property portfolio to extend the maturity of the EUR 142m facility for 24 months. This is a portfolio of French properties on long term lease contracts to the likes of Carrefour and Arriva. The portfolio benefits from a strong rental income that enables full payment of interest and some amortisation of principal over the term. The Bank believes the extension is a good result for both the Bank and the shareholders as asset values are likely to improve in the near future.

### **2.2.5 Repayments and exits**

To date 32 loans have been realised with a total cash flow amounting to approx. ISK 63bn since October 2008, thereof 25 loans have been paid in full, amounting to approx. ISK 47bn. The other seven loans were partially repaid amounting to ISK 16bn.

Furthermore, out of the 32 loans, seven loans have been sold, thereof 5 somewhat below par. The loans sold somewhat below par are:

- Transaction in October 2008 to secure the liquidity position of the Bank.
- Subordinated mezzanine position in a highly leveraged distressed company sold above fair value as enterprise value broke in the senior debt.
- 2 loans sold in the spring for a price significantly higher than otherwise perceived market value. The company had been under strain and performing poorly.
- Loan to a company that went bankrupt and had no assets to sell. The Bank's recovery was through guarantees provided by owners of the company.

## 2.3 Derivatives

### Overview

There are total of 149 foreign counterparties in the derivatives portfolio which can be broken down as follows:

- 103 ISDA counterparties (in 92 ISDA agreements, as some are multi entity)
- 32 non-ISDA counterparties, i.e. the Bank's general terms and conditions counterparties
- 14 counterparties within the Bank's group, i.e. subsidiaries and branches

The number of transactions with foreign counterparties is less than 1,000. The vast majority of these are traded under the ISDA agreements, most of which have been terminated by the counterparty.

There are 224 domestic counterparties in the derivative portfolio which can be broken down as follows:

- 14 ISDA counterparties (mostly domestic financial institutions but also some large companies)
- 195 non-ISDA counterparties, i.e. the Bank's general terms and conditions counterparties
- 15 counterparties within the Bank's group, i.e. subsidiaries and branches

The number of transactions with domestic counterparties is over 1,600. The vast majority of these are traded under general market agreements and a minority under ISDA agreements.

### Appointment of advisors

The ResCom has retained Alvarez and Marsal ("A&M") to manage the overall process of the winding down of the derivatives book and execute a plan that will maximise recoveries. To do this A&M will work with and coordinate the work of the employees of the Bank along with external derivatives valuation specialists. Furthermore, the business law firm Olswang was appointed as an external legal counsel to work on the legal process associated with recoveries of the derivatives portfolio.

### The process

A predefined process has been implemented and is strictly followed with counterparties being prioritised based on their importance to the estate. 4 work streams have been defined for the derivatives recovery: Counterparty interaction, Valuations, Legal and Back office-Treasury. A further distinction was made between parties operating under ISDA agreements (predominantly international counterparties) and the Bank's General Terms (predominantly domestic counterparties).

Each stream is predominantly staffed by employees of the Bank supported by external advisors where specialist expertise is required. All streams follow a narrowly defined process to achieve resolution of the exposures involving systematic checks on the streams' output and a full audit trail. After legal due diligence and valuation analysis each individual proposal is submitted to the Bank's management for approval before proceeding.

Overall prioritisation has taken place across the portfolio, factoring in 'live' or 'terminated' agreements, payable or receivable as well as the counterparty credit rating.

The review of all high priority counterparties, those that will recoup the maximum value is expected to be completed this spring. The remaining transactions will be dealt with in order of their ability to return value to the Bank. However, the settlement process also depends on counterparties' co-operation. Some cases may drag on, especially those that go into litigation. The plan, by applying a strict prioritisation process, puts the highest emphasis on those transactions that will maximise recovery of funds to the Bank.

Oversight and control of the derivatives process is ensured by the requirement to have the Bank's management sign-off at key stages in the interaction with counterparties, i.e. strategy for recovery, initiation of contact, agreement of amounts with counterparty and a decision to litigate. A full audit trail is maintained per counterparty.

***Open derivatives***

There are open derivatives both in the domestic and the foreign derivatives book and the total number of open derivatives contracts is less than 200. The transactions concern mainly plain vanilla interest rate swaps (IRS) and long term FX/Currency swaps with non-ISDA domestic counterparties. Process has been set up for a regular review in order to determine whether the positions should be kept or terminated in order to maximise the recovery of the contracts.

## 2.4 Overview of the Bank's branches and subsidiaries

The ResCom has conducted a substantial amount of work abroad to: i) secure the future business of entities, ii) restructure and sell off entities, iii) close down entities. Furthermore, members of the ResCom or its representatives have been nominated to replace former representatives of the Bank in subsidiaries which are still effectively controlled by the Bank.

### 2.4.1 Subsidiaries: Current status

Foreign subsidiaries of the Bank and their branches are directly responsible for the deposits made with them. These entities are not governed by Icelandic law. The rights of depositors regarding deposits made with a subsidiary of the Bank or branch of a subsidiary will be determined by the law and regulations applicable to that entity.

The table below summarizes the status of majority of the subsidiaries of the Bank.

Name of subsidiary	Current status
Arion Bank	Operational and 87% of its share capital owned by the Bank
FIH	Operational and owned by the Bank
Norvestia	Operational and partly owned by the Bank
Kaupthing Bank Sweden	Partially sold and its remainder wound down and assets transferred to the Bank
KSF	In administration
Kaupthing Singer & Friedlander (Isle of Man) Ltd.	In liquidation
Kaupthing Bank Luxembourg (KT Lux)	Dissolved
Kaupthing New York Inc.	Dissolved
Kaupthing Kabushiki Kaisha (Japan)	Has been wound down
Kaupthing (Hong Kong) Limited	In liquidation

More details on the subsidiaries are provided below.

**Arion Bank**, a commercial bank with operations in Iceland is a subsidiary of the Bank. On 6 October 2008 the Disbursement Act was passed by the Icelandic parliament, providing the FME with the authority and power to intervene in the operations of financial undertakings in order to respond to the unusual circumstances in the Icelandic financial sector. On 9 October 2008, in accordance with the same act, the FME appointed the ResCom to take control of the Bank. On 21 October 2008, the FME issued the Transfer Decision, by which it determined that certain specific assets of the Bank and certain specific obligations of the Bank were transferred to Arion Bank. According to the FME, these actions were taken to secure the continuation of vitally important domestic banking and payment services.

Under the Transfer Decision, Arion Bank took over the entire Bank's deposit liabilities in Iceland, and also the bulk of the Bank's assets that relate to its Icelandic operations, such as loans and other claims. Other assets and liabilities remained in the Bank and therefore under the control of the ResCom.

The FME appointed Deloitte to prepare an independent net asset valuation for Arion Bank and Oliver Wyman was appointed to co-ordinate the valuation process and review the valuation. The valuation of the net assets by Deloitte and the review of the valuation by Oliver Wyman took longer than initially envisaged but was completed towards the end of April 2009.

PwC audited the asset transfer from the Bank to Arion Bank to ensure that it was completed in full accordance with the FME transfer decision. PwC concluded that some assets that were initially moved to Arion Bank should have stayed with the Bank. Hence, this was corrected and these assets increased the size of the corporate loan portfolio of the Bank. It should be added that all cash flow to and from the assets since the FME transfer decision was made were corrected for between the two banks. ResCom supported these amendments as they are in full accordance with the FME transfer decision and the Committee consider these assets to be above average quality of the Bank's assets.

Total of approx. ISK 190bn in assets at book value were transferred back, thereof approx. ISK 90bn which were unpledged. These assets present additional value to the creditors, but instead negatively affected the size of the compensation instrument. The liabilities related to the pledged assets had remained within the Bank based on the preliminary balance sheets.

ResCom with its financial advisor, Morgan Stanley and creditors' representatives, negotiated with the Government during the summer 2009 on the disposition of the assets and liabilities taken over by Arion Bank in October 2008. ResCom entered into a Heads of Terms Agreement with the Government on 17 July 2009 and signed binding agreements on 3 September 2009.

On 1 December ResCom announced its decision regarding Arion Bank. ResCom, in consultation with the creditors and supported by its financial advisor throughout the process, decided that the Bank and thereby its creditors acquires 87% of common equity in Arion Bank. The Government will continue to own 13% of common equity. ResCom believes that active ownership of Arion Bank will maximize the value of assets which were transferred between the banks. As part of the agreement ResCom contributed ISK 66 billion to the capitalization.

Key points of the agreement:

- The Bank acquired 87% of the share capital in Arion Bank and 13% remain under Government ownership.
- ResCom contributed ISK 66 billion in common equity instead of the Government.
- Arion Bank remains governed by Icelandic law and Icelandic supervisory institutions ensuring deposits held in the bank remain as secure as before.
- Arion Bank is an independent operating subsidiary of the Bank.
- Kaupthing's subsidiary, Kaupskil ehf. holds Kaupthing's voting rights in Arion and appoints four members to the board of Arion Bank and the Government one.

The common equity of Arion Bank is approximately ISK 72 billion and the Tier I ratio 12%. The bank is fully capitalized and its liquidity position is strong. The bank has been profitable since it was established in October 2008. With the ResCom's involvement, Arion Bank is a strong bank and well positioned to lead the development of the Icelandic economy for the good of Icelandic people and domestic companies as well as its owners. The agreement with the Government entails that the Government contributes a subordinated, FX denominated loan which will increase Arion Bank's capital ratio to 16%.

Further information on this entity can be found at [www.arionbanki.is](http://www.arionbanki.is).

**FIH** is a subsidiary wholly owned by the Bank. It is a Danish full service corporate & investment bank focussing on lending to Danish companies. The entity was acquired by the Bank in 2004. The entity is fully operational and is currently not in a sales process. The Bank remains the sole shareholder of FIH and two representatives of the ResCom are board members. The ICB holds the entity's shares of the Bank as pledge against a EUR 500m loan. The board of directors of FIH has adopted a plan to adjust and focus FIH's future activities to meet the current market situation of the financial sector. As part of this adjustment, FIH has closed down the equities trading, research and wealth management department. These business areas were not expected to contribute positively to FIH's earnings on a short-term or a medium-term basis. In the future, FIH will focus on the core business areas: loans to corporate customers supplemented by two advisory units: Corporate Finance (FIH Partners) and Financial Solutions (advisory related to strategic risk management and liability management).

Further information on this entity can be found at [www.fih.dk](http://www.fih.dk).

**Norvestia Oyj** is a Finnish publicly listed Investment Company. The Bank owns approx. 32% of the outstanding shares and holds 56% of the voting rights. ResCom has two representatives on the board. Initially, the ResCom received offers for the Bank's shares in Norvestia which were about 40% lower than the net asset value. The ResCom concluded that the offered price was unacceptable and decided to hold on to the shares. Since then, the Bank has received EUR 1.25m dividend payment and the share price has risen about 30%. Furthermore, more feasible offers have been received, indicating that the value of the Bank's stake has increased by approx. EUR 25m. As for all other assets, Norvestia is monitored on a constant basis regarding further valuation upside and monetization options.

Further information on this entity can be found at [www.norvestia.fi](http://www.norvestia.fi).

**Kaupthing Bank Sweden** was a subsidiary wholly owned by the Bank, through Kaupthing Sweden AB. Following the opening of a Stockholm branch in September 2000, the Bank acquired both the Swedish securities firm Aragon and JP Nordiska Bank in 2002. Those acquisitions became the foundation for the Swedish operation, which grew organically in the years to follow. Kaupthing Bank Sweden offered integrated financial services to institutional investors, companies and (high net worth) individuals. These services included corporate banking, investment banking, capital markets services, asset management and comprehensive wealth management for private banking clients.

After 9 October 2008, ResCom managed to keep the entity operational. Without ResCom's co-operation with Riksbanken, the Swedish Central Bank, and the Swedish Financial Authorities (Finansinspektionen), the entity would most likely have been closed down and the assets sold at a fire sale to cover the liabilities. Instead the ResCom managed to dispose of certain assets after a structured sales process while other assets were transferred to the Bank.

Shortly after the fall of the Bank, Kaupthing Pension Consulting and Kaupthing Finans AB were sold as these business lines did not constitute a core business for Kaupthing Sweden and the latter would have required continued financial support. At the end of March, the ResCom closed a transaction with Ålandsbanken Abp where the latter acquired the private banking, capital markets and asset management assets of Kaupthing Bank Sweden. The private banking, asset management and capital markets businesses had substantial funding needs in 2009 which did not align well with the current status of the Bank.

ResCom believes that the transaction with Ålandsbanken Abp constitutes a good deal for the Bank as the sale price was reasonable and enabled Kaupthing Bank Sweden to pay 100% of subordinated loans to the Bank of some SEK 6bn (through transfer of assets worth SEK 6bn) and around 50% of its equity. This transaction also freed up cash for the Bank since Riksbanken returned to the Bank EUR 170m it had pledged, plus Icelandic government bonds and bonds issued by the Icelandic Housing Financing Fund of ISK 9.5bn.

The corporate loan portfolio and some other loans and equity positions have been moved to the Bank as a payment for the subordinated loan and are now under management by the Nordic asset management team of the Banks. These assets fit well with the other asset pools the Bank is currently managing. This portfolio accounted for the majority of the Swedish corporate banking assets of the Bank.

Deposits held by Kaupthing Sweden have been repaid to depositors. The repayment was originally funded with a loan from Riksbanken, the Swedish Central Bank but the above mentioned sale to Ålandsbanken allowed for immediate repayment of the facility. This facility was put in place in early October last year by Riksbanken in order for Kaupthing Bank Sweden to be able to pay back all deposits. Riksbanken was very co-operative but a repayment was required at the earliest convenience.

If the entity had not been sold, there is a substantial risk that only the deposits which had already been paid and perhaps the Riksbanken's facility could be repaid. However, this solution enabled the Bank to settle the Riksbanken facility as well as retrieving a sizable loan portfolio. In case of a bankruptcy of the entity, the recovery of the subordinated loan had presumably been very low, there would have been uncertainty over how much the Bank had retrieved from the Swedish Central Bank and the equity would have been worthless. The result of the transaction is therefore that assets of approx. EUR 800m at nominal value were retrieved.

Further information on this entity can be found at [www.kaupthing.se](http://www.kaupthing.se).

**Kaupthing Singer & Friedlander ("KSF")** was a wholly owned subsidiary of the Bank, acquired in 2005. It was an established bank in the UK offering integrated financial services to companies, institutional investors and individuals. These services included corporate banking, investment banking, treasury services, and comprehensive wealth management services for private banking clients.

On 8 October 2008, KSF was taken into administration and Maggie Mills, Tom Burton, Alan Bloom and Patrick Brazzill of Ernst & Young, UK, were appointed as administrators. Kaupthing EDGE UK was transferred by the UK Treasury to ING Group and later the same day, the entity was put into administration on the application of the FSA.

The assets and liabilities of KSF are not part of the estate and the ResCom is not responsible for the administration. Further information on this entity can be found on the liquidators' website [www.kaupthingsingers.co.uk](http://www.kaupthingsingers.co.uk).

**Kaupthing Singer & Friedlander (Isle of Man) Limited** was a wholly owned subsidiary of the Bank. The entity carried out traditional banking activities as well as asset management activities for a broad spectrum of corporate and private customers along.

At a hearing in the Isle of Man High Court on Wednesday 27 May 2009, a Winding-up Order was made placing the Company into liquidation. Michael Simpson of PricewaterhouseCoopers and Peter Spratt of PricewaterhouseCoopers (London) were appointed as joint provisional liquidators of the entity and Joint Deemed Official Receiver at that time.

The assets and liabilities of KSF IoM are not part of the estate and the ResCom is not responsible for the administration. Further information on this entity can be found on the administrators' website [www.kaupthingsingers.co.im](http://www.kaupthingsingers.co.im).

**Kaupthing Bank Luxembourg S.A. ("KT Lux")** was a wholly owned subsidiary of the Bank. *Kaupthing Bank Belgium* and *Kaupthing Bank Luxembourg, Geneva Branch* were branches of KT Lux. The main services offered at KT Lux were private banking and wealth management. On 9 October 2008, KT Lux's board of directors applied for a suspension of payments status with the Luxembourg District Court sitting in commercial matters. KT Lux was granted this status and its management was monitored by administrators. The Court appointed PricewaterhouseCoopers Luxembourg, represented by Mrs Emmanuelle Caruel-Henniaux and Mr Franz Fayot, to act as KT Lux's administrators. This decision also applied to the Belgian branch of KT Lux.

KT Lux together with its management designed a restructuring plan approved by its creditors and the Luxembourg District Court. The plan involved a corporate restructuring of KT Lux, resulting in dividing it up. As of 13 July 2009 the banking operations were transferred to Banque Havilland S.A., a newly-created Luxembourg company which provides private banking service. Furthermore, some of KT Lux assets and liabilities were moved to a securitisation company called Pillar Securitisation S.à r.l. Due to

this division, KT Lux was dissolved without being liquidated and the administration period is therefore over.

The assets and liabilities of KT Lux are not part of the estate and the ResCom is not responsible for the administration.

**Kaupthing New York Inc** was a wholly owned subsidiary of the Bank established in 2000. The entity focused on securities brokerage and investment banking. The entity, as well as two other subsidiaries of the Bank in the United States, has been dissolved.

**Kaupthing Kabushiki Kaisha (Japan)** has been wound down without the need for any insolvency proceeding.

**Kaupthing (Hong Kong) Limited** is in insolvent liquidation.

**2.4.2 Branches: Current status**

According to the Disbursement Act, deposits made by private individuals and companies are priority claims. Whether the legislation applies to depositors depends on which entity in the Kaupthing Group they were deposited with. The legislation only applies to Icelandic financial undertakings. The Bank has repaid all deposits made at foreign branches belonging to the Bank which are defined by Icelandic law as priority claims.

The table below summarizes the status of some of the branches of the Bank.

Name of branch	Current status
Kaupthing EDGE Austria	Has been wound down and is in the process of being deregistered
Kaupthing Bank Finland	Has been wound down and assets transferred to the Bank
Kaupthing EDGE Germany	Has been wound down and deregistered
Kaupthing Bank Norway	Under administration and assets transferred to the Bank
Kaupthing Bank Sweden	Is being wound down and has been deregistered
Kaupthing Bank Dubai and Qatar	Has been wound down and is in the process of being deregistered

Furthermore, the Bank had branches in Italy, France, the United Kingdom, the Netherlands, Spain and the Faroe Islands. These branches were not conducting banking operation in October 2008 and what limited functions they had at that time have since been wound down in all material respects. More details on the branches listed in the table above are provided below.

**Kaupthing EDGE Austria** was a branch of the Bank. It was established in 2008 and offered competitive solutions for depositors. Depositors have now been paid back. The entity has been wound down and is in the process of being deregistered.

**Kaupthing Bank Finland** was a branch of the Bank. The branch offered a wide range of investment banking services to companies, institutions and wealthy private individuals. Following the appointment of the ResCom the Finnish FSA took charge of the branch on 9 October 2008. A few days after 9 October 2008, ResCom managed to prevent the entity from going into administration along with the associated potential fire sale of assets to protect the asset base of the

Bank. In co-operation with the Finnish authorities, the ResCom negotiated loans to the entity with three commercial banks in Finland which were guaranteed in part by the Finnish authorities. This enabled the entity to repay deposits in the branch. The credit portfolio and certain other assets of Kaupthing Bank Finland were pledged against these loans. There was a pressure to sell assets to repay the loans from the local banks and the Bank's local operations were disrupted and proactive management of assets suffered. The asset management operation was sold as well as a part of the loan portfolio. The remaining part of the loan portfolio has been transferred to the Bank and is now managed by the asset management team. The branch was closed down at the end of January 2009. Had the entity ended up in administration, the assets of the entity would have been sold in order to pay back depositors and it is unlikely that any assets would have been transferred to the Bank in Iceland. Therefore, ResCom believes that this was the best solution for the Bank as it prevented potential fire sale of assets and instead, assets of approx. EUR 107m at nominal value were transferred and consolidated on the balance sheet in Iceland.

**Kaupthing EDGE Germany** was a branch of the Bank. It was established in 2008 and offered competitive solutions for depositors. The operation was seized by the German government, and its assets frozen by the German Financial Regulatory Authority, BaFin. On 22 June 2009 the BaFin lifted its freeze on the assets of the Bank.

Since 2008, the Bank worked hard in co-operation with the German authorities to develop a solution which fully ensured the secure repayment of deposits to the Bank's customers. DZ Bank AG, which was appointed as the payment agent for the entity's customers, seized EUR 55m, which in the opinion of the Bank should have been used to reimburse the entity's depositors. Litigations on this matter are ongoing.

In mid-April 2009, the Bank announced that it had secured sufficient funds to reimburse all Edge deposits in Germany. In mid-May the Bank was ready to start the repayment process and sent letters to more than 34,000 depositors.

On 22 June 2009, the repayment process commenced and was completed by the end of the year. Repayments to Edge depositors in Germany amounted to approx. EUR 322m.

**Kaupthing Bank Norway** was a branch of the Bank. Kaupthing entered the market in Norway in 2003, when the Bank acquired Tyren Holding AS, an asset management company. The branch provided comprehensive financial services including asset management, in a separate entity, and private banking to wealthy private individuals, investment banking and capital markets services to companies, institutional investors and private clients. In addition, it had started to provide their clients with banking services, adding retail banking and corporate banking to its range of services.

On 11 October 2008, the Norwegian government placed a freezing order on the assets of the entity and related companies and placed the operation of the branch under administration. In co-operation with the Norwegian government, ResCom managed to prevent the immediate sale of assets from the entity, including the Bank's position in Storebrand, which would have been done to pay back depositors. Instead, the deposits held by the branch were repaid to depositors by the Norwegian Banks' Guarantee Fund. In February, the ResCom and the administrators in Norway reached an amicable agreement which included release of the assets which were under administration in Norway. As a result, the majority of the corporate loan portfolio has been transferred to the Bank in Iceland and other assets saved from imminent fire sale. This agreement also prevented lengthy and very costly process of dealing with the administrators and netting the entity. If the ResCom had not managed to prevent the immediate sale of assets from the entity, the entity had presumably only been able to pay back part of the deposits and no assets would have been left to be transferred to the parent company. The result is that imminent fire sale of assets was prevented which resulted in retrieval of assets of approx. EUR 365m at nominal value.

**Kaupthing Bank Sweden** was a branch of the Bank in Sweden. It held the EDGE deposits in Sweden which have been repaid as described above in the clause on the Swedish subsidiary. The branch is in the process of being wound down and has been deregistered.

**Kaupthing Bank Dubai and Qatar** was two branches of the Bank, one in the Dubai International Financial Centre and one in the Qatar Financial Centre, both established in 2007. The branches focussed on providing investment banking services in the region. The ongoing operations of the branches have been sold to the Bank's previous management in Dubai and Qatar. The proceeds from the sale are held by the Bank.

## 2.5 Other Assets

### **Storebrand**

In December 2009 the Bank sold its 24,700,000 shares in Storebrand ASA representing an aggregate of 5.5% of the share capital of the company. The selling price was determined in an accelerated book built offering. The shares were sold to institutional investors. Following the transaction, the Bank and its affiliates do not own any further shares in Storebrand.

The imminent potential asset sales in October 2008 would have included the Bank's position in Storebrand (approx. 5.5% of outstanding shares) at NOK 10 per share. However, the ResCom managed to reach an agreement with the Norwegian administrators allowing the Bank to hold on to its shares for more than a year.

The ResCom followed the movements of the stock very closely during the year. When the price approached NOK 40 per share the ResCom sought advice from banks and securities firms on potential sale of the shares. At that time analysts had set a target price for the stock in the range of NOK 40-45 per share and by setting its target price at NOK 40 per share the ResCom was securing a 3 fold return on what otherwise would have been cash deposits if the Norwegian administrator had completed his sales process. In a favourable market trend, the ResCom finally sold its shares successfully on 1 December 2009.

The selling price was NOK 39 per share (only 2.5% discount to closing of NOK 40 per share). The price was below NOK 40 per share for the following month but has in the past weeks risen above that level.

If the shares had been sold by the administrator in late 2008, the proceeds would have amounted to NOK 247m or EUR 25m (2008 year-end FX). However, the proceeds when the ResCom sold the shares in December 2009 amounted to NOK 963 or EUR 116m (2009 year-end FX).

Therefore, the gain of holding on to the shares is approx. 290% measured in NOK and approx. 360% if measured in EUR.

The Bank received quotes from large banks and brokerage firms on the potential sale of its holding. An agreement was reached with Morgan Stanley which engaged Carnegie and Enskilda to assist in the sales process.

## 2.6 Operating cost

The table below shows the operating cost of the Bank, i.e. for both the ResCom and the Winding-up Committee, for the year 2009. The reason for higher salary cost in Q4 is due to significant increase in number of employees in Finance, less outsourcing to Arion Bank, and temporary increase in number of employees during the claim filing process. The increase in fees paid to external advisors is primarily due to external advisory work on the derivatives side and external advisory work related to the agreement on Arion Bank.

(ISKm)	Q1	Q2	Q3	Q4	Total
Salaries and salary related cost	66	105	137	229	537
External advisors	406	594	875	1.350	3.225
Thereof domestic	89	171	259	375	894
Thereof foreign	317	423	616	975	2.331
Other expenses	37	76	139	72	324
<b>Total</b>	<b>509</b>	<b>775</b>	<b>1.151</b>	<b>1.651</b>	<b>4.086</b>

- The cost of realisation for 2009 was approx. 0.24% of gross AuM\* (ISK 1.706bn at fair value as at 30 June 2009).
- Internal operating cost in 2009 is fully covered by fees received on the 'Loans to customers' portfolio.
- External advisory cost in restructuring exercises is in many cases borne by the borrower.

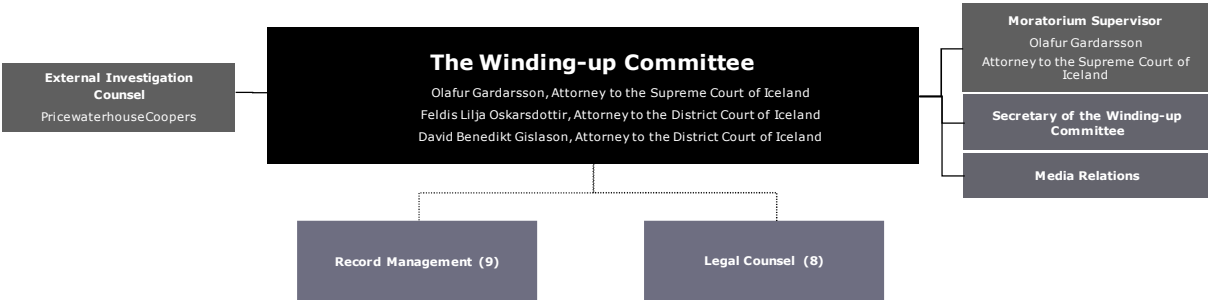
\* Gross AuM = Total assets as at 30 June 2009 where impairments have been taken into account.

### 3. The Claiming Process

#### 3.1 The Winding-up Committee

On 25 May 2009, the Reykjavík District Court approved a request from the ResCom and appointed a Winding-up Committee for the Bank, as provided for in Act No. 44/2009, amending the Act on Financial Undertakings. Olafur Gardarsson, Supreme Court Attorney and the Bank’s moratorium supervisor, District Court Attorney Feldis Lilja Oskarsdottir and District Court Attorney Davíð Benedikt Gislason were appointed to the Winding-up Committee. The ResCom and Winding-up Committee jointly direct the Bank’s affairs, cf. the divisions of tasks provided for in Points 3 and 4 of Temporary Provision V of the Act on Financial Undertakings. The appointment of the Winding-up Committee allowed the formal process of filing claims to begin, while ResCom continues to perform its role of safeguarding the Bank’s assets in order to ensure that as much as possible is received for claims.

Below is an organization chart for the Winding-up Committee.



The Winding-up Committee administers the formal process of filing claims, handles all claims against the Bank and makes decisions regarding their recognition. The Committee invited creditors of Kaupthing bank to lodge their claims in writing within six months of the first publication of a formal notice in the Icelandic Legal Gazette (*Lögbirtingablaðið*) on 30 June 2009. Accordingly, the deadline to lodge claims was 30 December 2009. Once the time limit for lodging claims expired the Winding-up Committee compiled a list of claims lodged. The Winding-up Committee shall make independent decisions on recognising claims, including the priority given to them. This process has started and will be ongoing in the coming months.

At the end of set time limit for the filing of claims, the Winding-up Committee held a creditors' meeting on Friday 29 January 2010 at Hilton Reykjavik Nordica. The list of lodged claims was made available to creditors one week prior to the meeting, on 22 January 2010, on a secure website and at the offices of the Winding-up Committee at Borgartun 26 in Reykjavik.

A creditor, who is unwilling to accept the Winding-up Committee's decision as regards the recognition of his/her claim against the Bank, shall state his objections at a creditors' meeting or notify the Winding-up Committee in a letter received by it no later than at that meeting. In the same manner, a creditor may object to the Winding-up Committee’s position on the recognition of a claim filed by another creditor if the conclusion regarding the claim affects the interests of the objecting party. Insofar as no objection is raised against the Winding-up Committee’s decision on the recognition of a claim, its decision shall be regarded as approved.

The list of claims was presented at the creditors’ meeting, as well as any objections which the Winding-up Committee received in regard to lodged claims. At the creditors’ meeting, the Winding-up Committee provided those in attendance with the explanations as to the recognition of claims and any objections which have been made against recognition of specific claims, as well as the reasons for its decision towards the recognition of those claims. If an objection is raised at the meeting against the Winding-up Committee’s decision on the recognition of a claim, the Winding-up Committee shall endeavour to settle the dispute. If such a dispute cannot be resolved at the creditors' meeting, the Winding-up Committee shall convene a separate meeting between the disputing parties. If the dispute cannot be resolved at such separate meetings, then the dispute will be referred to the District

Court of Reykjavík. As far as protests are not made against the recognition of claims, then such recognition shall be considered accepted.

### 3.2 Summary of lodged claims

A total of 28.167 claims were lodged against the Bank by the deadline for lodging claims on 30 December 2009. Claims received after the expiration of the time limit are not entered in the list of claims.

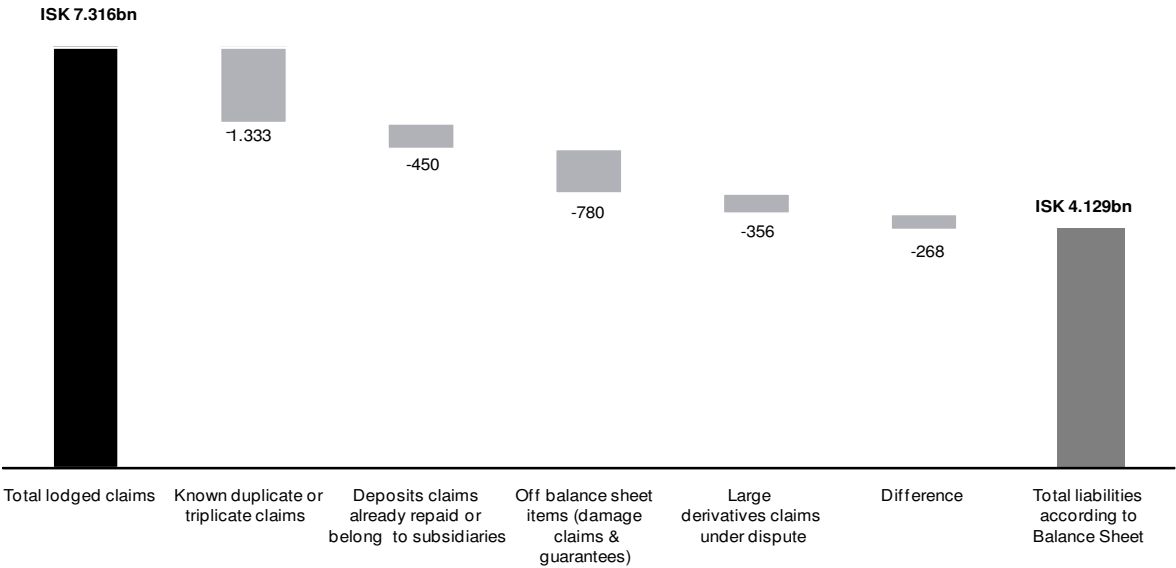
Below is a summary of the total amount of lodged claims. All amounts are in ISK.

Total amount of claims lodged pursuant to Art. 109:	88.486.388.393
Total amount of claims lodged pursuant to Art. 110:	398.506.301.333
Total amount of claims lodged pursuant to Art. 111:	321.710.496.507
Total amount of claims lodged pursuant to Art. 112:	1.210.200.637.303
Total amount of claims lodged pursuant to Art. 113:	4.805.863.416.200
Total amount of claims lodged pursuant to Art. 114:	491.458.638.557
Total amount of claims lodged:	<u>7.316.225.878.293</u>

The total amount of claims lodged is ISK 7,316 billion, at the ISK exchange rates of the Central Bank of Iceland on 22 April 2009. The aggregate amount of claims exceeds the Bank's liabilities as recognised in its balance sheet of 30 June 2009. The difference can in part be explained by claims lodged for deposits which the Bank has already repaid, significant amount of bond claims and some deposits claims lodged in duplicate or triplicate, off-balance sheet items, such as claims for damages and guarantees. Furthermore, creditors generally lodge claims at maximum levels. The aforementioned claims add up to at least ISK 2,900 billion.

The large number of claims lodged the bank, has necessitated postponing decisions on certain claims. A follow-up creditors' meeting to continue discussion of lodged claims will be held on 18 May 2010, at 10:00 AM at Hilton Reykjavik Nordica. At this meeting the Winding-up Committee plans to present its decision on claims on which a decision has not been made prior to the meeting on 29 January 2010, insofar as it is possible. The Winding-up Committee, furthermore, plans to hold a second follow-up creditors' meeting in 2010 to continue presentation of its decisions on lodged claims. The Winding-up Committee will attempt to conclude its decision on all claims prior to that meeting. Having regard for the final sentence of the first paragraph of Art. 119 of the Bankruptcy Act, no decisions will be taken on subordinate claims.

**Bridge from lodged claims to total liabilities according to Balance Sheet as at 30 June 2009**



The above-mentioned amounts are put forth for informational purposes only and do not reflect the decisions of the Winding-up Committee on individual claims. The above figures are solely provided to give an indicative overview of the difference between the amounts of lodged claims and liabilities presented in the bank's balance sheet of 30 June 2009. Large majority of claims are still to be made, and therefore, the bridge from lodged claims above is neither final nor exhaustive. Considering the amount of claims lodged in duplicate so far, further duplicates can be expected. In many cases lodged amounts and the legitimacy of claims are under dispute, thereof large amount of derivatives claims. In some cases, creditors lodge aggregate amounts as opposed to net amounts. Furthermore, in several cases, creditors lodge claims at maximum levels. Until final decisions on lodged claims have been made, the exact amount of liabilities is uncertain.

A further discussion on lodged claims can be found on the Winding-up Committee's secure website for creditors.

## 4. Legal status and process going forward

### 4.1 *The moratorium process*

On 21 November 2008 the ResCom filed an application with the District Court of Reykjavik, pursuant to Bankruptcy Act to stay creditor actions in order to facilitate the financial reorganization of the Bank. On 24 November 2008 the Bank was first granted a moratorium on debt payments until 13 February 2009. Later an extension was granted from 13 February 2009 until 13 November 2009. Furthermore, on 13 November 2009, the Bank's ResCom and the Moratorium Supervisor requested a further extension, and on 19 November the District Court of Reykjavik granted the Bank an extension of moratorium until 13 August 2010.

Applying for the moratorium in November 2008 was, in the opinion of the ResCom, a necessary step to gain protection from litigation, collection measures and other depletion of assets and to ensure that all creditors of the Bank are treated fairly and appropriately in accordance with Icelandic law through the protection of the Bank's assets. The Bank will, upon the conclusion of the moratorium, automatically enter into winding-up proceedings.

According to the recent amendments to the Act on Financial Undertakings, the Bank's protection against litigation, enforcement, collection measures and other depletion of assets obtained under the moratorium will continue to exist when the Bank formally enters a winding-up process, Olafur Gardarsson, Attorney to the Supreme Court of Iceland was appointed as the Moratorium Supervisor. He has been a Supreme Court Attorney since 1992 and his areas of expertise include mergers and acquisitions, corporate and telecommunications law.

### 4.2 *Overview of the moratorium legislation*

The provisions governing the moratorium have been amended by Act no. 44/2009 which came into force on 22 April 2009. The Bank remains under the direction of the ResCom which is responsible for the daily operations of the Bank in accordance with Act no. 44/2009 but remains also under the supervision of the Moratorium Supervisor. The ResCom holds the powers of the board of directors as well as the powers of the Bank's shareholders' meeting according to new provisions. Formerly the ResCom held only the powers of the board of directors on the grounds of the decision of the FME of 8 October 2008. The Bank remains subject to Act No. 161/2002 on Financial Undertakings and the general supervision of the FME. The District Court of Reykjavik however has exclusive jurisdiction over the enforcement of the moratorium, its extension and termination etc.

The provisions of Act no. 44/2009 stipulate that the ResCom shall manage the interests of the Bank according to the same rules as a trustee would be subject to according to the Bankruptcy Act, although with some exceptions. The exceptions mainly concern the objective for the ResCom to maximise the value of the Bank's assets which includes waiting for the Bank's outstanding claims to mature, instead of realising them immediately. To this end, the ResCom is allowed to disregard a decision of a creditors' meeting if the ResCom deems such a decision contrary to its objective of maximizing asset value. This means that the ResCom has ample time to safeguard the interests of the Bank and its creditors.

The reference to provisions governing the actions of a trustee under the Bankruptcy Act entail that the ResCom has the capacity to manage the Bank's assets and it alone can dispose of its assets and answer for its obligations. The ResCom acts for the Bank in court and executes agreements on behalf of the Bank as before. The ResCom shall make sure that all assets are disposed of in the most efficient manner possible and shall enforce all claims owned by the Bank. The ResCom furthermore takes such actions as necessary to prevent damage to the Bank.

The ResCom can convene creditors' meetings as appropriate to introduce measures taken in regard to the Bank's interests. In such meetings suggestions or decisions may be sought from creditors in regard to measures which have yet to be taken and suggestions may be sought on matters regarding the management of the Bank's interests. The creditors' meeting cannot influence measures which have already been taken by the ResCom, only such measures which have yet to be realised. The

ResCom is allowed to consult with individual creditors in matters concerning the relevant creditor's interests.

A petition for the Bank to enter insolvent liquidation cannot be filed nor can its assets become subject to an attachment, an execution or a forced sale while the moratorium remains in effect. No law suit can be commenced against the Bank while the moratorium is in effect unless such action is specifically provided for by law or relates to criminal proceedings.

The ResCom is committed to protecting the interests of creditors by preventing the provisional attachment or freezing of assets. The moratorium has provided the Bank with appropriate protection from legal actions, such as the freezing of assets. In the European Economic Area the Bank seeks recognition of the moratorium on a case-by-case basis on grounds of the EU Winding-Up Directive No. 2001/24/EC. The Bank has also been granted recognition and injunctive relief under Chapter 15 of the United States Bankruptcy Code. This has provided the Bank with protection for its assets in the United States. The ResCom has successfully opposed freezing orders in the United States, Luxembourg, Germany, Finland, Austria and the Netherlands. Without the moratorium, preventing proposed freezing orders could be considerably more difficult for the Bank.

The Bank will, upon the conclusion of the moratorium, automatically enter into winding-up proceedings unless all the Bank's obligations have been fully paid or composition reached with creditors. Following the changes of the Icelandic legal system, with the adoption of the above Act. No. 44/2009, the current moratorium is based on the main rules, principles and characteristics of winding-up proceedings. There is negligible difference in legislation applying to Kaupthing whether in moratorium or winding-up proceedings. If the Bank enters into winding-up proceedings, the ResCom shall continue to manage the interests of the Bank and maximize value for the benefit of creditors. Winding-up proceedings can conclude in composition with creditors or an insolvent liquidation, cf. also below.

According to the Act no. 44/2009, the Bank's protection against litigation, enforcement, collection measures and other depletion of assets obtained under the moratorium will continue to exist when the Bank formally enters a winding-up process,

### *4.3 Potential closing of the moratorium process*

As previously outlined, the Bank was first granted a moratorium on debt payments and a license for financial reorganization in a court hearing on 24 November 2008. The District Court can currently not authorize a moratorium lasting longer than a total of 24 months from the court hearing, i.e. until 24 November 2010.

The moratorium process of the Bank shall conclude by means of one of the following:

- i) Winding-up proceedings

When an authorisation for moratorium concludes, a financial undertaking shall enter a winding-up process according to Act no. 44/2009 amending Act no. 161/2002 on Financial Undertakings unless the Bank's obligations have all been fully paid or composition reached with creditors. Many of the rules governing the moratorium, and which are mentioned above, would continue to apply in a winding-up process. The ResCom continues to operate under a winding-up process with the same aim as before to maximise the value of assets. That includes waiting for the maturity of assets rather than disposing of them immediately.

If in the winding-up process, the assets of the Bank are found to be of less value than the amount of its liabilities there are two possibilities to conclude the Bank's operations, i.e. insolvent liquidation or a composition with creditors as described below. Act no. 44/2009 also provides for the conclusion of the Bank's operations through insolvent liquidation or a composition with creditors without an intermediate winding-up process. This applies if the ResCom and the Winding-up Committee can decide whether, and if so to what extent, the assets of the Bank are found to be of less value than the amount of its liabilities, before the moratorium expires.

## ii) Insolvent liquidation

In a state of insolvency liquidation, the management of the assets of the Bank would vest in a liquidator. Claims against a bankruptcy estate denominated in foreign currency shall be converted into the Icelandic currency at the selling rate posted on 22 April 2009 and it is very likely that a trustee in bankruptcy will convert all liquid assets into the Icelandic currency in the event of insolvency in order to transfer the currency risk from the estate to the Bank's creditors. Such a measure would be understandable from the point of view of the trustee of the estate, but it may not be in the interests of the Bank's creditors.

According to the Bankruptcy Act, the trustee in bankruptcy shall ensure that the winding-up is concluded without undue delay. As stated above the ResCom and the Moratorium Supervisor believe that the interests of the creditors are best served by restructuring the Bank's operations. It is therefore clear that the obligations of the trustee in bankruptcy according to the article may prevent this from happening. In addition, a Bank in insolvent liquidation would forfeit its banking license, face forced asset sales, and have less flexibility to support its assets. It is likely that performing loans to customers as well as listed and unlisted assets would be sold at a substantial discount.

It is the opinion of the Moratorium Supervisor and the ResCom that this option would minimize debt recovery for the creditors of the Bank and it would not be in their best interests.

## iii) Composition with Creditors (Scheme of Arrangement)

A composition with creditors seeks to solve a debtor's financial difficulties by proportionally reducing creditors' claims but at the same time allows the debtor to stay solvent. This arrangement endeavours to maximize debt recovery and preserves creditors' interest by granting the debtor the opportunity to be restructured and support assets instead of being forced into an immediate sale of assets. If the moratorium process of the Bank were to be concluded by arrangement composition with creditors, potential restructuring options of the Bank can be considered and evaluated.

The minimum creditor support required for a scheme of arrangement is 60% in terms of value and the number of creditors voting. Claims are converted into Icelandic krona as of 22 April 2009 but distributions can be in any currency specified under the scheme.

It should be pointed out that the ResCom is working towards a solution whereby the restructuring of the Bank will be completed by a Composition with creditors in order to prevent the Bank from entering insolvency proceedings, which could reduce the value of assets.

## 4.4 Icelandic composition legislation overview

### 4.4.1 Introduction

The composition with creditors in the Bank's case follows largely the same legal approach as if it were conducted under insolvency proceedings. The main difference being that there is no requirement for Kaupthing to seek prior approval of at least 25% of creditors' both by number of creditors and the total amount of claims.

This overview, focuses exclusively on the rules applicable to Kaupthing and general rules applicable to compositions of creditors shall not be considered except as they apply to Kaupthing.

The key concept of the composition with creditors is that it is an agreement on the payment or release of debt obligations which is binding on all creditors holding composition claims, provided that certain majority of creditors holding composition claims has approved the composition proposal. The composition with creditors seeks to make the Bank solvent through the release of debt obligations, rather than disposition of assets and financial reorganisation which the moratorium was intended to provide for.

#### 4.4.2 *Composition Claims*

##### **Calculation of Composition Claims**

Composition claims shall be converted to Icelandic krona at Icelandic Central Bank selling rate as at 22 April 2009. Composition claims shall otherwise be calculated as at 22 April 2009, including accrued interest, indexation, foreign exchange effects and other ancillary claims accumulated at that time. According to the aforesaid, the calculation of composition claims should be in line with the claims as submitted in the claim filing process where 22 April 2009 was the cut-off date for interest etc.

#### 4.4.3 *Composition Proposal*

The Bank will prepare a composition proposal. It must state to what extent the debtor offers payment of the composition claims and the form of payments, the dates of the payments, whether interest, and if so, at what rate, will be paid on the composition claims from the date a composition agreement is concluded and until the date of payment, if deferred payment is envisaged, whether security, and if so of what kind, will be placed to secure performance of the composition agreement.

#### 4.4.4 *Creditors' Meeting to consider Composition Proposal*

##### **Convening of Creditors' Meeting**

Once the Bank is satisfied that the composition proposal can be put to a vote by creditors, a special creditors' meeting shall be summoned by the publishing of a notice to that effect at least two weeks prior to the Creditors' Meeting. The notice shall be published in the Icelandic Legal Gazette (*Lögbirtingablaðið*).

The Winding-up Committee shall prepare a register of the rights to vote on the proposal, specifying the voting rights attached to composition claims. The number of creditors shall be stated as well as the percentage amounts attached to each composition claim. The register shall include only the claims that have been recognised and to which voting rights are attached in the opinion of the Winding-up Committee.

##### **Voting**

The composition proposal must be approved by the same proportion of votes as the proportion of composition claims to be released according to the composition proposal, provided this reaches 60% at a minimum, by number of voting creditors as well as 60% of the amounts of composition claims belonging to voting creditors. If neither proportional nor total release of debt obligations is proposed, the composition proposal must be approved by at least 60% of all voting creditors by number as well as of the 60% amounts of composition claims belonging to voting creditors.

Example: If 75% of all composition claims shall be released according to the composition proposal, then the composition proposal must be approved by at least 75% of all voting creditors by number as well as 75% of the amounts of composition claims belonging to voting creditors

Voting creditors can vote on the composition proposal in writing and shall such votes be tallied if they reach the Winding-up Committee before end of voting at the creditors' meeting, so long as no one is present on behalf of the creditor to vote on his behalf. A vote submitted in writing must fulfil certain requirements, such as signatures having been witnessed etc. Creditors can grant a power of attorney to a representative as well.

##### **Effects of Disputed Votes**

Votes shall be counted immediately at the creditors' meeting. The votes shall first be counted as to determine whether a result can be obtained even if all disputed votes are taken into effect. If all disputed votes, were they to be admitted and counted, could not alter the result of the voting, then the voting results shall be final.

If disputed votes, were they to be admitted and counted, could affect the voting results, the Winding-up Committee shall endeavour to resolve the dispute if all the disputing parties are present. If they are not present, then the Winding-up Committee shall convene a separate meeting with the disputing

parties in an effort to solve the dispute. If the dispute cannot be solved, the Winding-up Committee shall forward the argument to the District Court of Reykjavík to be ruled on.

Forwarding disputes to the District Court of Reykjavík can delay the process but, depending on when the composition proposal will be voted on, the court will already have decided on a number of claims through the claims filing process before the composition proposal is voted on.

#### **4.4.5 Legal Effect of Composition**

If the composition proposal is approved by the creditors, the Winding-up Committee must obtain a confirmation of the District Court of Reykjavík of the composition agreement. The composition agreement shall take effect when Winding-up Committee's submission for confirmation has been approved by a final court decision, by the District Court of Reykjavík or the Supreme Court of Iceland.

The composition agreement shall be binding on creditors and their successors in regard to their composition claims. The composition agreement does not affect a creditors' right to enforce security or guarantees granted by third parties.

#### **4.4.6 Composition Agreement not approved or court confirmation rejected**

If the composition proposal is not approved by the creditors or its confirmation has been rejected, the Winding-up Committee shall request that the undertaking enters into an insolvent liquidation. A creditor may do the same if its claim has been recognised in the winding-up proceedings and either the composition negotiations have not yielded any results or the creditor demonstrates that the legal requirements for composition negotiations to take place are not fulfilled or that such a large number of creditors are opposed to composition that there is no possibility of achieving composition based on available information on the undertaking's financial situation. In order to uphold this claim, the creditor must, however, establish a legitimate interest for the insolvency proceedings to go ahead rather than continuing the winding-up proceedings.

### **4.5 Creditors' meetings**

According to the new Act no. 44/2009 the matters considered at creditors' meetings are mainly twofold, firstly there are matters concerning the management of the ResCom of the interests of the Bank and secondly, the recognition of claims by the Winding-up Committee.

The ResCom can convene creditors' meetings, as it deems appropriate, to introduce measures taken in regard to the Bank's interests. The ResCom may seek proposals or decisions regarding measures that have yet to be taken, and provide for opportunities for making such proposals. The creditors' meeting cannot affect measures already carried out by the ResCom. The ResCom is allowed to confer with individual creditors in matters concerning the relevant creditors' interests.

A creditor is entitled to attend a creditors' meeting if the creditor has filed a claim against the Bank with the Winding-up Committee and if such claim has not been finally dismissed by the Winding-up Committee. Creditors' meetings regarding the management of the Bank's interests and the recognition claims will not be held until the deadline for filing claims has passed. If a creditor does not attend a meeting, the relevant creditor may lose the right to oppose matters or present claims regarding matters which were decided or presented at the meeting.

Voting rights are determined by the amount of each creditors claim if matters regarding the management of the Bank's interests are put to a vote. For a creditors' meeting to be quorate, creditors holding at least a third of the total voting rights must be present at the meeting. To disregard a decision of the majority of creditors, the ResCom must in most cases have specific reasons for doing so. The ResCom can thus disregard decisions of a creditors' meeting if they are contrary to law, dishonest, cannot be executed, contrary to interests of creditors not attending, discriminate against the minority or if the decisions are contrary to the goal of maximising the value of the Bank's assets.

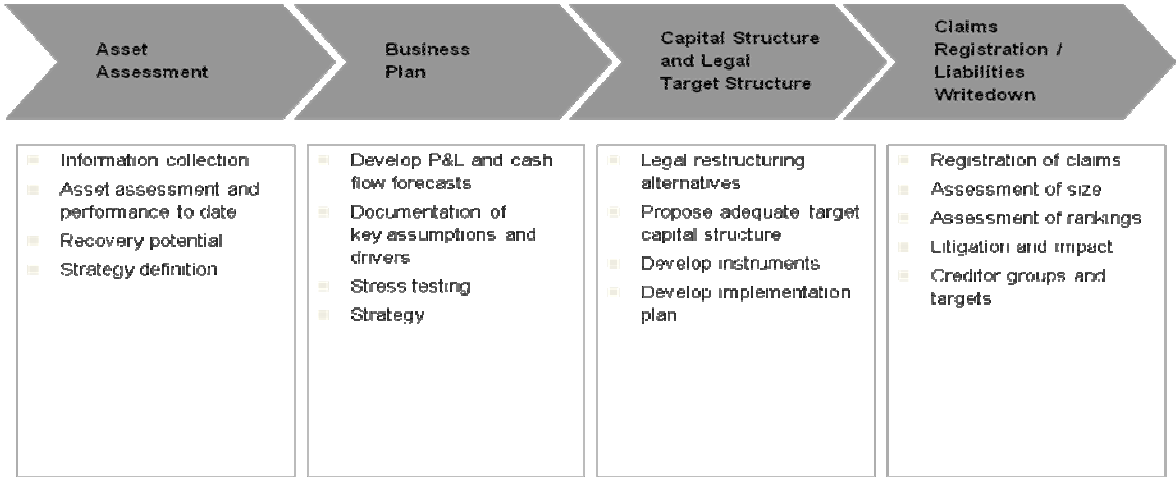
### 4.6 Overall restructuring and distribution to creditors

The ResCom believes that the interests of the creditors are best served by restructuring the Bank's operations.

The ResCom has been working on solutions to preserve and increase the value of the assets. In many cases, the assets need to be held for some time for them to be redeemed at acceptable value. The moratorium or the winding-up process following the moratorium will end either through scheme of arrangement or insolvent liquidation of the Bank. Therefore, the ResCom has requested that Morgan Stanley, its financial advisor, assist in developing structuring ideas on how the assets can be passed over to creditors at a later stage. All these ideas should aim at providing ongoing support to the assets and building a structure where creditors can exit their holdings over time.

**Work streams**

Work has commenced on the various parts of the restructuring (see work streams below). The eventual timing is subject to the progress of the winding-up proceedings and depends on how substantial disputed claims will be and the time it will take to settle these disputes.

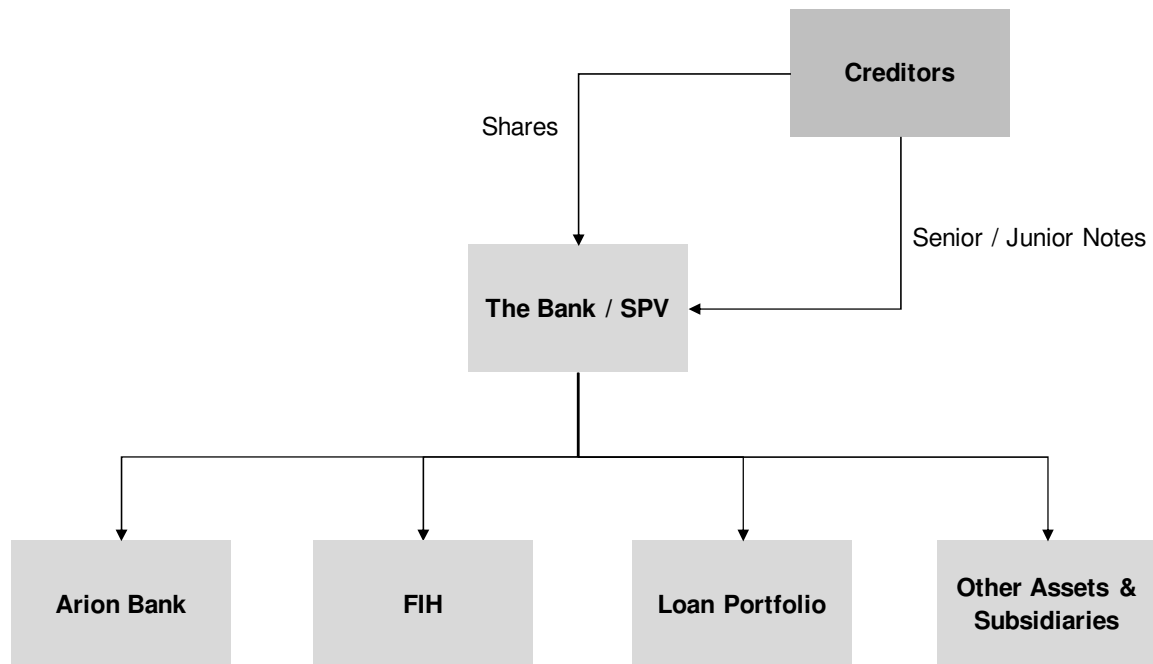


*Work streams.*

**Target structure for the Bank**

- After scheme of arrangement the Bank operates as a parent company or as new SPV as ongoing asset management company.
- Value realization for creditors through convergence of claims into cash distribution and issuance of instruments.
- Strategy focused on value maximization through cash collection, separate monetization of holdings and work out of other assets.

A graph of a potential target structure for the Bank can be seen on the next page.



*Potential target structure for the Bank.*

***The Bank's overall restructuring***

The ResCom is focused on finding the best possible closure for all relevant parties in a realistic time frame and distributing the resulting value to creditors.

It is currently uncertain when distribution or partial payments can be made to creditors or an attempt made to reach composition agreements. The eventual timing is subject to the progress of the winding-up proceedings which is administered by the Bank's Winding up Committee. According to the report presented by the Winding-up Committee to a creditor meeting held on 29 January 2010, composition cannot be sought and partial payments of general claims cannot be made until review of, and decisions made by the Winding-up Committee on the major portion of claims covered by Articles 109-112 is complete and, as the case may be, resolution of any disputes by the relevant courts is concluded.

Further information on issues concerning the process of lodging claims and decisions by the Winding-up Committee on claims lodged can be found on the Winding-up Committee's secure website for creditors.

## 4.7 Future communication with creditors

The publication of the list of lodged claims presented a good opportunity to reorganise creditor communications and introduce new processes for information disclosure. The Creditors' Report will continue to be published on regular basis on the Bank's website to keep creditors informed of the latest progress of the Bank's operations.

Additionally, there will be quarterly (or event-driven) Creditors' Report Update Meetings with dial-in opportunity for creditors. These meetings will be held following the publications of the Creditors' Report. Questions will have to be sent in advance. As announced on the Bank's website, the first such meeting will be held on 15 March 2010 at 4pm GMT, at the offices of Morgan Stanley, 20 Bank Street, Canary Wharf, London E14 4AD.

Creditors interested in attending the meeting or dial-in are required to confirm their interest by sending an e-mail stating the names of creditors and representatives to [creditorcontact@kaupthing.com](mailto:creditorcontact@kaupthing.com) by midnight GMT on 10 March. It must be clearly stated whether representatives will be attending in person or calling in. Dial-in information will only be provided upon request.

Questions MUST be sent in advance to [creditorcontact@kaupthing.com](mailto:creditorcontact@kaupthing.com) by midnight GMT on 10 March. Creditors are urged to state their questions as clearly and concisely as possible. Please note that the Creditors' Report Update Meeting is held to allow creditors to ask questions regarding the latest update of the Creditors' Report, e.g. the year-end figures. Creditors are encouraged to keep that in mind when questions are submitted. For various reasons, including bank secrecy and commercial sensitivity, information on certain matters cannot be released.

Initially, the Informal Creditors' Committee ("ICC") was composed of representatives of the Bank's largest known creditors and included a broad cross section of financial institutions. The members of the ICC were chosen in co-operation with the ResCom's former advisor Deloitte LLP. The selection was primarily based on the value and the nature of the creditors' claims as well as geography. The ICC did not have formal powers or duties under Icelandic law and was consultative in nature. The ICC was established to have a set-up for creditors to provide direct feedback to the ResCom. The ResCom extends gratitude to all ICC members for their active participation and helpful contribution to date.

### **New creditors' committee**

The claims registration process has been completed and a significant change in the composition of the group of creditors is noticeable. The ResCom is now to establish a new platform to ensure a constructive dialogue with creditor representatives. The ResCom believes that this is the right time to restructure the ICC and give other creditors or group of creditors the opportunity to join a new creditors' committee. The deadline for applications has passed. Information about members of the new creditors' committee will be published on the Bank's website in due course.

The new creditors' committee will comprise approx. 3-6 representatives, each representing a creditor or a group of creditors (each representative can have an alternate representative).

The selection will be based on overall size of represented claims and validity of claims and overall representation of type of creditors in the creditors' committee.

Other things to keep in mind regarding the creditors' committee's members:

- Signing of NDA as members will be exposed to material non-public information likely restricting members from being able to trade.
- No compensation to members of creditors' committee for travelling etc.
- Members acting for a group of creditors can pass on information to disclosed parties they represent as long as these parties have signed respective NDA.

[The selection process is ongoing and a new creditors' committee will be announced shortly on the Bank's website.](#)



## Appendices

### *A1 Meeting minutes: Creditors' Meeting held 5 February 2009*

#### **Minutes recorded by Kaupthing Bank's Moratorium Supervisor at a creditors' meeting, cf. Art. 14 of the Icelandic Act no. 21/1991 on Bankruptcy etc.**

A meeting was held on Thursday 5 February 2009 at 10:00 a.m. at Hilton Reykjavík Nordica, Sudurlandsbraut 2 in Reykjavík, with the creditors of Kaupthing Bank hf., Borgartún 19, 105 Reykjavík, ID-No. 560882-0419, concerning the bank's authorisation for a moratorium.

Olafur Gardarsson, Attorney to the Supreme Court of Iceland, Moratorium Supervisor, chaired the meeting and recorded the minutes, cf. Art. 14 paragraph 2 of Icelandic Act no. 21/1991. The meeting was called in accordance with the provisions of Article 98, paragraph 3 of the Act no.161/2002 on Financial Undertakings, cf. Act no 129/2008.

The meeting was attended by representatives of the bank's creditors, a total of 250 people. Given that the majority of those present did not speak Icelandic it was decided that the main section of the meeting would be held in English. Tomas Jonsson, Attorney to the Supreme Court of Iceland, helped the Moratorium Supervisor chair the meeting. The Bank's ResCom was also present to answer questions.

The Moratorium Supervisor gave a report on the assets and liabilities as of the reference date, explained how he believed the debtor's finances could be reorganised and described what measures had already been taken in this respect. Those attending the meeting received a copy of a presentation, and a detailed summary in English and Icelandic by the Moratorium Supervisor was also distributed.

The Moratorium Supervisor announced his proposal that an application be made to extend the moratorium by nine months at the next hearing of the Reykjavík District Court which is to be held on 13 February at 2:00 p.m.

The Moratorium Supervisor then sought the views of the creditors on his actions and proposals for action. When the Moratorium Supervisor had finished, creditors were given the opportunity to ask questions and put across their points of view. Twenty-one people raised questions.

Questions were raised concerning various topics which had been discussed in the Moratorium Supervisor's presentation and the Moratorium Supervisor and members of the ResCom answered these questions as far as they were able. A summary of the questions raised and the committee members' replies is enclosed with these minutes. A German investor speaking on behalf of more than 800 German deposit holders declared the group's support for the extension of the bank's moratorium. A letter was also presented from two creditors in which they agreed to the extension but only for a further three months.

No objections were raised to the extension of the moratorium. The Moratorium Supervisor asked the meeting twice whether anybody objected to applying for an extension to the moratorium. No objections were raised.

At the end of the meeting the Moratorium Supervisor presented the main points from the minutes to the meeting and invited those present to add any remarks they may have. The minutes were approved in their current form.

The meeting was adjourned at 12.15 p.m.  
Ólafur Gardarsson

## A2 Meeting minutes: Creditors' Meeting held 20 October 2009

registration no. of Kaupthing Bank hf. 560882-0419;

meeting jointly held by

i) Kaupthing Bank's ResCom, according to Article 103, Paragraph 3 of Act no. 161/2002 on Financial Undertakings, cf. Act no. 44/2009 and Temporary Provisions to Act no. 44/2009;

ii) and Kaupthing Bank's Moratorium Supervisor cf. Chapter 2 of Act no. 21/1991 on Bankruptcy etc., cf. Article 2 and 4 of Act no. 129/2008, still in effect according to the provisions of Article 10, Paragraph 2, of Act no. 44/2009 (both Acts amending Act no. 161/2002 on Financial Undertakings).

The meeting was held at Hilton Reykjavik Nordica, Suðurlandsbraut 2 in Reykjavík, on October 20, 2009, and commenced at 10 am.

Registered at the meeting were 104 representatives of creditors.

Members of the panel at the meeting were:

Tómas Jónsson, Attorney to the Supreme Court, Chairman of the meeting.

Ólafur Gardarsson, the Moratorium Supervisor and member of Kaupthing's Bank Winding-up Committee.

Steinar Thór Gudgeirsson, Chairman of the ResCom.

Knútur Thórhallsson, Deputy Chairman of the ResCom (during items 1, 2)

Theodór Sigurbergsson, member of the ResCom.

Eva Sóley Gudbjörnsdóttir, Managing Director of Finance, Kaupthing Bank.

Kolbeinn Árnason, Managing Director of Legal, Kaupthing Bank.

Dieter Turowski, representative of Kaupthing's exclusive financial advisor Morgan Stanley.

Karsten Hofacker, representative of Kaupthing's exclusive financial advisor Morgan Stanley.

Halldór Bjarkar Lúdvígsson, Managing Director of Asset Management – Nordic Portfolio, Kaupthing Bank (during items 1-2, 6).

Dominic McCahill, representative of Weil Gotshal & Manges, legal advisors to Kaupthing (during items 1-2, 4-6).

Finnur Sveinbjörnsson, CEO of Arion Bank (during items 3-6).

Björk Thórarinsdóttir, Managing Director of Credit, Arion Bank (during item 4-6).

### 1. Introduction

Ólafur Gardarsson welcomed the creditors.

The main purpose of the meeting is to provide creditors with an update on key events and activities since the last meeting in February, to provide creditors with the latest financial information on the Bank, to provide creditors with an overview of the processes and a summary of the Capitalization Agreement on Arion Bank, to outline the next steps and restructuring options of the Bank and to discuss the possible extension of the Bank's moratorium on debt payments. According to Icelandic law, no binding decisions can be made at the meeting.

Tómas Jónsson, Attorney to the Supreme Court of Iceland, was asked to serve as chairman of the meeting. He assumed the duties of the chairman and confirmed that the meeting was called as prescribed by law. Given that the majority of those present did not speak Icelandic it was decided that the meeting would be held in English.

### 2. Key Events and Progress during the Moratorium

#### 2.A. Key Milestones

Steinar Thór Gudgeirsson presented key milestones. Steinar discussed the general approach of the ResCom, which ultimate task and duty is to maximize the value of the Bank's assets and pass on the value to its creditors. Steinar presented a summary of the Bank's balance sheet and the status of maximizing the value of the assets. Steinar furthermore discussed the status of the Bank's subsidiaries and branches and the organizational structure of the Bank.

## **2.B. Loan Restructuring / Europe and Nordic**

Halldór Bjarkar Lúdvígsson presented an overview of the loan restructuring in the Europe portfolio (fair value as at 30 June 2009 approx. 140 bn ISK) and Nordic portfolio (fair value as at 30 June 2009 approx. 170 bn ISK). The mandate of the asset management division can be broken into five steps, which were discussed: stabilization, consolidation, full overview, which leads to management of the assets and ends with *value optimization and exit strategy*. Halldór presented an overview of loans to customers by portfolio and sector, as well as a past cash-flow analysis. According to his presentation, a considerable part of the Nordic and Europe portfolios has undergone major restructuring and Halldór discussed the Bank's restructuring principles and core values. In all major cases the Bank has relied on valuation work or input by third party advisors. Halldór furthermore discussed actions taken on the portfolios and the progress with the restructuring work, as well as giving an overview of full repayments and exits.

## **2.C. Financial Information Update**

Eva Sóley Guðbjörnsdóttir presented an update on the financial information of the Bank, including information on the Bank's balance sheet, cash in hand, development of loans to customers at fair value and information on derivatives.

## **3. Capitalisation Agreement on Arion Bank**

### **3.A. Overview of Agreements with the Government**

Kolbeinn Árnason presented an overview of the agreements with the Government relating to Arion Bank and discussed the two options available to the Bank. The ResCom has the sole power to decide whether to choose option 1 (Kaupthing to acquire Arion Bank) or option 2 (Government retains Arion Bank). Kolbeinn presented a summary of the key terms of both options. According to option 1, Kaupthing would receive an 87% ownership following a capitalization contribution of 65% (ISK Cash and Icelandic related assets), approx. equalling 66 bn ISK (ownership might possibly be increased to 90% under option 1). According to option 2, Kaupthing would have the right to repurchase 90% of the equity from the Government during the exercise period of one month following the publication of the annual report for the years 2010-2014. Kolbeinn also discussed Kaupthing's consultation with creditors and creditors' due diligence. For further details, reference is made to Kolbeinn's presentation and further publicly available information.

### **3.B. Presentation of Arion Bank**

Finnur Sveinbjörnsson presented an overview of Arion Bank. Finnur presented the balance sheet and income statement of Arion Bank, as well as a cash flow analysis. He also discussed Arion Bank's five year business plan and presented an analysis of the loan portfolio. Finnur furthermore discussed the recovery process within Arion Bank, including a breakdown of recovery cases by sectors. Finnur discussed the current liquidity position of Arion Bank and the FX imbalance. Finally Finnur discussed the upside potential of Arion Bank and the importance of ownership for the next few months.

### **3.C. Due diligence and Summary / Review of Capitalisation Options**

Karsten Hofacker presented a summary of due diligence on Arion Bank carried out by Kaupthing and its advisors. Due diligence is ongoing, as audit of financials is not yet completed. Due diligence to date has focused on balance sheet analysis / net asset valuation of Arion Bank, detailed analysis of the business plan, liquidity risk and profit improvement measures. Karsten discussed a summary of the valuation and a returns profile with regards to the two options.

Dieter Turowski presented an overview of the pros and cons with regards to the two options.

### **3.D. Creditor Consultation Process**

Max Ziff, representative of Houlihan Lokey, discussed the due diligence on Arion Bank assets and the choice between the two options previously presented (option 1 and option 2).

Chip Fisher from Bingham McCutchen, representing a group of bond holders, and a member of the Informal Creditors' Committee (ICC) and the ICC Sub-Committee, discussed Kaupthing Bank's creditor consultation process. Chip expressed his view that he was happy with the work of the ResCom with respect to guarding the interests of creditors.

A lunch break was made at 12.45 pm.

During the lunch break creditors were invited to submit written questions for the following Q&A session.

The meeting commenced again at 1.20 pm.

#### **4. Morgan Stanley overview**

John Hepburn, from Morgan Stanley, discussed the role of Morgan Stanley with regards to the work of the ResCom.

#### **5. Next Steps and Restructuring Options**

##### **5.A. Legal Overview**

Ólafur Gardarsson discussed the Bank's moratorium and gave a legal overview of the moratorium process. The first moratorium was granted from 24 November 2008 until 13 February 2009. According to the Icelandic legislation, the moratorium can be granted for up to 24 months. An extension was granted from 13 February 2009 until 13 November 2009 and another extension of 9 months will be requested on 13 November 2009. The moratorium can be concluded in the following ways, which were discussed by Ólafur: (1) Winding-up process pursuant to Act no. 44/2009; (2) Composition of creditors (Scheme of arrangement); (3) Insolvent liquidation.

##### **5.B. Overall Restructuring**

Dieter Turowski discussed the work streams of the restructuring process of Kaupthing Bank.

Karsten Hofacker discussed the target structure for the Bank, the current legal paths for restructuring as well as the liability restructuring.

##### **5.C. Moratorium Extension**

Ólafur Gardarsson announced his proposal that an application be made to extend the moratorium by nine months at the next hearing of the Reykjavik District Court which is to be held on 13 November 2009. The arguments presented included the fact that a Chapter 15 protection in the USA might be terminated should the moratorium not be extended. Ólafur then sought the views of the creditors on this proposal, in accordance with the Act on Bankruptcy etc.

Arnar Thór Jónsson from the law firm Réttur, acting on behalf of more than twenty bank creditors, presented concerns and objections to the capitalisation agreement. A formal letter to the ResCom was also received by the chairman from the law firm, detailing the concerns and objections further.

No objections were made to the extension of the moratorium.

#### **6. Q&A**

Questions submitted during the lunch break were addressed by panellists (one question was also addressed by Gisli Óttarsson, Managing Director of Risk Management at Arion Bank). Any remaining questions will be dealt with in due course and published on the website. Unanswered questions directed to Arion Bank regarding SPM will be dealt with by Arion Bank.

Following this Dominic McCahill discussed the ruling of the High Court of England today, relating to Kaupthing's application for judicial review of the legitimacy of the decision taken by the UK Treasury to transfer assets and deposits from Kaupthing Edge accounts at Kaupthing Singer and Friedlander in October 2008. The Court held that the UK Treasury had acted within its statutory powers and there had been no error in its decision-making process.

The chairman of the meeting presented the main points from the minutes to the meeting and invited those present to comment on them. No comments were made.

Steinar Thór Gudgeirsson adjourned the meeting.

The meeting was adjourned at 3 pm.

Minutes recorded by Kaupthing Bank's Moratorium Supervisor, cf. Act no. 21/1991 on Bankruptcy etc.

### A3 Exchange rates

Exchange rates for ISK against all major currencies as at 31 December 2009, 30 June 2009 and 31 December 2008.

	<b>31.12.2009</b>	<b>30.6.2009</b>	<b>31.12.2008</b>
AUD .....	112,53	102,90	84,46
CAD .....	119,74	109,91	98,72
CHF .....	121,18	117,78	113,82
DKK .....	24,16	24,04	22,73
EUR .....	179,78	179,04	169,27
GBP .....	202,65	210,04	176,48
JPY .....	1,35	1,32	1,34
NOK .....	21,63	19,84	17,39
SEK .....	17,54	16,52	15,44
USD .....	125,43	127,56	121,10

## A4 Initial tasks of the ResCom

At its inception, the ResCom had the objectives laid out below. Some of these objectives were set with reference to the Disbursement Act. However, it should be noted that the ResCom played no part in determining the creation of Arion Bank.

**Maintaining the Bank's commercial banking operations in Iceland** in line with the Disbursement Act. The ResCom worked hard to ensure that the daily operations of the Bank's branches were not significantly affected. This objective was reached when Arion Bank was formally established on 18 October 2008 and took over the Bank's commercial banking operation in Iceland on 22 October 2008.

**Protecting depositors both domestically & overseas in accordance with the Disbursement Act.** The ResCom co-operated abroad with governments, financial authorities and central banks. This objective was achieved domestically, where Arion Bank is now responsible for domestic deposits and, abroad where According to the Disbursement Act, deposits received by the Bank or its branches are priority claims against the Bank. The Bank is thus under an obligation to repay these deposits prior to non-priority claims. Icelandic law does not affect the repayment of deposits received by subsidiaries or their branches. Possible repayment of those deposits is the concern of the boards of directors or administrators of the relevant subsidiaries.

**Ensuring cash flow in all currencies both domestically and to/from foreign jurisdictions.** The difficulties that were experienced with payments to and from Iceland were primarily due to the actions of foreign governments and foreign currency restrictions imposed by the ICB. Efficient movement of capital was vital for the Icelandic economy. These difficulties were resolved in part with the Transfer Decision.

**Ensuring expertise and knowledge by hiring key employees.** One of the main tasks of the ResCom is to safeguard the value of the Bank's assets until they have been transferred to creditors. In order to achieve this aim, there must be sufficient expertise in place to manage the assets and provide the necessary services. This objective was achieved through the appointment of several qualified full-time and part-time employees. Around 65 employees now work for the ResCom, supported by an external advisory service as needed to ensure expertise in every case.

**Finalizing the Bank's balance sheet.** The aggregate balance sheet has been divided between the Bank and Arion Bank as at 22 October 2008. Separate balance sheets for the Bank and Arion Bank had to be prepared. Financial disclosure and financial information is an ongoing process, financial information for the Bank as of 30 June 2009 and 30 December 2008 can be seen in chapter 2 *Financial analysis*.

**Preserving the interests of creditors.** The ResCom has focused from the outset on protecting the assets of the Bank and preserving value for creditors. Creditors have been informed of developments via the Bank's website, creditor contact address and press releases. This objective is an ongoing task and will not be fully attained until a permanent solution for the assets, satisfactory to the creditors of the Bank has been identified and executed.

### **Prevent the provisional attachment of assets and facilitate the retrieval of the Bank's assets**

The ResCom is committed to protect the interests of creditors by preventing litigations, the provisional attachment or freezing orders on assets. In the European Economic Area the Bank seeks recognition of the moratorium on a case-by-case basis on grounds of the EU Winding-Up Directive No. 2001/24/EC. The Bank has also been granted an injunctive relief and the moratorium recognized as a foreign main proceeding under Chapter 15 of the United States Bankruptcy Code. This has provided the Bank with protection for its assets in the United States. The ResCom has also facilitated the release of assets through negotiations with local authorities or private parties in several countries.

### **Collecting claims and enforcing securities**

The Bank continues to enforce rights against its debtors in case of non-performance of obligations. That includes enforcing pledges and other securities, taking control of relevant entities etc.

***Ensuring expertise and knowledge by hiring key employees.*** One of the main tasks of the ResCom is to safeguard the value of the Bank's assets until they have been transferred to creditors. In order to achieve this aim, there must be sufficient expertise in place to manage the assets and provide the necessary services. This objective was achieved through the appointment of several qualified full-time and part-time employees. Around 65 employees now work for the ResCom, supported by an external advisory service as needed to ensure expertise in every case.

## Disclaimer

This report (including all subsequent amendments and additions) was prepared by the Resolution Committee ("ResCom") for the creditors of Kaupthing Bank hf. ("the Bank") for information purposes only. It should give creditors an overview of the background, the current situation and the potential steps going forward. The additions and amendments to this report since the previously published versions of this report are intended to give the creditors information on recent developments but are not necessarily and should not be regarded as an exhaustive list of all developments which creditors may consider material. In preparing and updating this report, the Bank has not taken account of the interest of any particular creditor or group of creditors.

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This report does not include an estimate of the likely level of recoveries for creditors. Very material uncertainties continue to exist regarding the timing and realisable value of assets and the eventual level of creditors' claims. The Resolution Committee wish to caution creditors against using the data in this report to estimate likely recovery as any such estimates are likely to be materially misleading. The actual realisable value of the Bank's assets and liabilities may differ materially from the values set forth herein. Factors which may lead to material differences include:

- (a) Resolution of issues regarding the quantum of claims
- (b) The realisation method(s) used over time
- (c) The impact of set off and netting including in connection with derivative contracts
- (d) Movements in currency exchange rates and interest rates
- (e) Prevailing market conditions when assets are sold

Nothing in this report should be relied upon by any person for any purposes including, without limitation, in connection with trading decisions relating to the Bank. Neither the Bank, the Resolution Committee, the Winding-up Committee, nor the Moratorium Supervisor accepts any responsibility for any such reliance.

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