

Andrew Caldwell

*Independent Valuer appointed by HM Treasury under
The Northern Rock plc Compensation Scheme Order 2008*

13 November 2008

Dear Sir or Madam

Independent Valuation under the Northern Rock plc Compensation Scheme Order

I was appointed by HM Treasury on 8 September 2008 as Independent Valuer under the Northern Rock plc Compensation Scheme Order 2008¹ ("the Compensation Scheme Order"). It is my role to determine the amount of any compensation payable by HM Treasury to the persons specified in Part 2 of the Compensation Scheme.

The role of the Independent Valuer is to conduct a fair, open and transparent valuation in accordance with the Compensation Scheme. It is consistent with this role that I proceed with reasonable speed.

In order to assist me in my role I have assembled a team of people to support me, including:

- my team of valuation experts at BDO Stoy Hayward LLP;
- Panmure Gordon & Co who will support me by providing such information concerning the banking, securities and financial assets markets as I may consider necessary or helpful to enable me to undertake the valuation; and
- Mayer Brown International LLP who will provide me with legal advice as I require it.

The following categories of parties will have been affected by The Northern Rock plc Transfer Order 2008 ("the Transfer Order"):

- those who held ordinary, foundation or preference shares in Northern Rock plc;
- those whose rights to receive shares in Northern Rock plc (whether by subscription, conversion or otherwise) were extinguished by Article 4 of the Transfer Order; and
- those whose consequential rights were extinguished by Article 12 of the Transfer Order.

In this letter, any person falling within one or more of the above categories is referred to as an "Affected Party". You have been currently identified by Northern Rock or its registrar, Capita Registrars, as an Affected Party.

In order to ensure that the valuation process is as fair and open as possible, I set out below an outline of the procedure that I propose to adopt. You will see that I am proposing a procedure in which I invite substantive submissions from Affected Parties and other relevant parties (the "Parties") as to the valuation of the shares. If you have any comments on either the proposed procedure itself or my proposed valuation approach (see below), I invite you to write to me with those comments within four weeks from the date of this letter. I will review and consider all the comments I have received within that period.

¹ SI 2008/718. This can be viewed at www.opsi.gov.uk

A. *Valuation assumptions*

Under Article 6 of the Compensation Scheme Order, I am required to assume, in determining the amount of any compensation payable by HM Treasury, that Northern Rock plc:

- is unable to continue as a going concern; and
- is in administration.

In addition, under s. 5 (4) of the Banking (Special Provisions) Act 2008², I am required to assume that:

- all financial assistance provided by the Bank of England or the Treasury to the deposit-taker in question has been withdrawn (whether by the making of a demand for repayment or otherwise); and
- no financial assistance would in future be provided by the Bank of England or the Treasury to the deposit-taker in question (apart from the ordinary market assistance offered by the Bank of England subject to its usual terms).

I am aware that there are proceedings pending before the Administrative Court in relation to these valuation assumptions. In particular, the claimants are seeking declarations against HM Treasury that the valuation assumptions which I am required to apply are incompatible with their rights to the peaceful enjoyment of possessions under Article 1 of Protocol 1 to the European Convention of Human Rights. I understand that a hearing has been listed in January 2009, but it is not known when the issues in the proceedings will be finally concluded. Taking into account the possibility of an appeal or appeals, the proceedings could be before the courts for a considerable time.

I have considered whether I should delay beginning my work until these proceedings are finally concluded, but I am not presently minded to do so, for two reasons. First, I consider that, in the interests of all Affected Parties and in the public interest, I should perform my role as speedily as is consistent with the proper exercise of my statutory functions. A delay pending the conclusion of possibly lengthy legal proceedings should be avoided if possible. Secondly, the information which I will wish my team to gather from Northern Rock plc and others (outlined below) is likely to be the same irrespective of the valuation assumptions to be applied. So there appears to be no good reason why the process of gathering that information should await the outcome of the legal proceedings.

B. *Approach to Valuation*

Meanwhile, based on the assumptions that I am required to apply, I propose to consider the likely market value of Northern Rock as a whole and also the realisable value of all assets and liabilities of Northern Rock as at 22 February 2008, the date at which the shares of Northern Rock were taken into temporary public ownership.

If you have any comments on the suitability of this approach in the context of the assumptions I am required to make, please provide me with those comments in writing within four weeks from the date of this letter.

C. *Valuation Process*

I propose to adopt the following process.

Stage 1: Finalise valuation procedure

- Consider comments received in response to this letter.

²This can be viewed at www.opsi.gov.uk

Stage 2: Request and obtain information relevant to the valuation process

- Obtain and review the following broad categories of documents:
 - information from Northern Rock as to the true value of the company's assets and liabilities; and
 - market information as to the prospect, and likely terms, of an open market sale of: (a) the whole business; (b) individual parts of the business; and (c) the assets of the business.
- Hold meetings with the Parties either individually and/or in representative groups, to allow them to make oral representations to me. The format and number of such meetings will depend on the number of individuals or groups who request a meeting.

Stage 3: Review and analyse the information obtained

- Review and analyse all the information received as a result of the work undertaken at Stage 2.
- Make available to all Affected Parties a document containing:
 - a description of the material obtained during Stage 2 of the valuation process;
 - an explanation of the information I consider can properly be disclosed to the Affected Parties (bearing in mind that the information that I expect to be provided by Northern Rock plc will include confidential and commercially sensitive material) together with details of the ways in which Parties can view the information;
 - the approach that I propose should be taken to determining the amount of any compensation payable by HM Treasury; and
 - my preliminary views on the valuation, based on that approach and on the material I have reviewed and considered.

Stage 4: Consultation

- Invite submissions on the matters addressed in the document within a specified timescale.

Stage 5: Review and analyse the information obtained

- Review, collate and consider the submissions made by Parties.
- Determine the amount of any compensation payable by HM Treasury to the persons specified in Part 2 of the Compensation Scheme.
- Prepare a Final Document to be sent to all Parties at the same time as the Assessment Notices (see stage 6 below).

The Final Document will set out my findings and the basis for them. It will also give some feedback regarding the consultation responses received and explain how those responses influenced my decision.

Stage 6: Notify all Affected Parties of any compensation payable and of their right to seek reconsideration of my decision

- Issue Assessment Notices to the Affected Parties setting out the amount of any compensation determined by me as being payable.
- Each Assessment Notice will be accompanied by a copy of my Final Document (see Stage 5 above).
- Each Assessment Notice will also be sent to the Treasury.

- Each Assessment Notice will contain details of the period within which and means by which Affected Parties may seek reconsideration of the Notice.

Stage 7: Reconsideration process

- Affected Parties may seek reconsideration within a set period;
- Where a request for reconsideration is made, the determination will be reconsidered and a revised Assessment Notice issued, which will contain notification that the original Assessment Notice has been upheld or varied, as the case may be, and details of the period within which and means by which any Affected Party dissatisfied with the revised Assessment Notice may refer the valuation to the Financial Services and Markets Tribunal.

Contact details

Any written correspondence should be addressed to:

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Independent Valuer under the Northern Rock plc Compensation Scheme Order 2008

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or through the website: www.northernrockvaluer.org.uk

or by fax: 020 7893 2329

If you have any queries about the matters in this letter, please contact the Northern Rock Valuer Helpline on 0800 3777 353.

Please be advised that any comments received on the proposed procedure may be published. If you would not like your comments to be published or included in any summary I may wish to produce, I should be grateful if you could make that clear in your comments and explain briefly why.

Yours faithfully,



Andrew Caldwell