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Case No: 7942 of 2008 and Case No: 16389 of 2009

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION

COMPANIES COURT

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 21 August 2009

Before :

MR JUSTICE BLACKBURNE

**IN THE MATTER OF LEHMAN BROTHERS INTERNATIONAL (EUROPE) (in
administration)**

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

AND IN THE MATTER OF THE COMPANIES ACT 2006

NUMBER 2

**William Trower QC and Daniel Bayfield (instructed by Linklaters LLP) for the
Administrators and LBIE**
**Richard Snowden QC and Andrew Thornton (instructed by Freshfields Bruckhaus
Deringer) for the London Investment Banking Association**
Anthony Zacaroli QC (instructed by Allen & Overy LLP) for the GLG Partners LP

Hearing dates: 29th and 30th July 2009

Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this
Judgment and that copies of this version as handed down may be treated as authentic.

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MR JUSTICE BLACKBURNE

Mr Justice Blackburne :

1. This application, brought both by way of ordinary application pursuant to paragraphs 63 and 68(2) of schedule B1 to the Insolvency Act 1986 and by way of a Part 8 claim form, is by the administrators of Lehman Brothers International (Europe). Its purpose is to establish whether a scheme of arrangement under Part 26 of the Companies Act 2006 (“the 2006 Act”) which the administrators wish to promote between LBIE and certain scheme creditors is one which the court has jurisdiction to sanction. If there is jurisdiction then the administrators seek a direction that they be at liberty to apply to the court for directions with a view to convening meetings of scheme creditors under section 896 of the 2006 Act.
2. The administrators who have appeared before me by Mr William Trower QC and Mr Daniel Bayfield recognise that because the only other persons represented before me are the London Investment Banking Association (“LIBA”), a trade association for firms in the investment banking and securities industry, and GLG Partners LP, which manages a number of hedge funds and is a member of a working group which has assisted the administrators in the preparation of the scheme, any view that I express on the question of jurisdiction cannot bind the very considerable number of former clients of LBIE who will qualify as scheme creditors under the scheme if I should conclude that there is jurisdiction and that the administrators should be at liberty to apply for the requisite meetings to be convened. It would be open to such persons to raise afresh the question of jurisdiction. That said, the proposal has attracted considerable support. The first hearing in relation to the proposed scheme (in March) was the subject of advance notice on the section of the PwC website dedicated to the administration of LBIE. It invited anyone who wished to attend or appear at that hearing to contact Linklaters LLP, who act for the administrators. One of the members of the scheme working group, GLG Partners LP, has appeared before me by Mr Antony Zacaroli QC to add its support to the submissions of Mr Trower and Mr Bayfield. But the proposal has met with opposition from LIBA which has been represented before me by Mr Richard Snowden QC and Mr Andrew Thornton. LIBA acknowledges the difficulties faced by the administrators but its view is that the court has no jurisdiction to sanction the scheme.
3. The Financial Services Authority, which is entitled to be heard, has chosen not to be represented before me. Instead, its General Counsel’s Division has sent a letter to Linklaters, stating that the FSA is supportive “in principle... of the use by the Administrators of mechanisms (including Schemes of Arrangement) that should lead to savings of time and money, provided that the particular mechanism delivers an appropriate degree of protection to consumers and others entitled to protection under FSMA 2000”. But the letter then goes on to say that “it would not expect to object to a Scheme that met [that] description... but cannot yet say that it does not object to the Scheme currently formulated”. It expressly takes no position on the issue of jurisdiction that has been debated before me.
4. The proposed scheme which, so far as I need to, I will describe in more detail later does not claim to be a fully worked-up scheme, ready to be presented to the intended creditors. Despite its length and detail (it runs to 86 pages and includes eight appendices and has obviously been the subject of a great deal of thought and very careful drafting), the document before me does not claim to be other than a summary of the principal terms and effect of what is proposed. Section 1 of the document

states why the scheme is being promoted. It is to set out the procedures which LBIE wishes to use “for the purpose of returning certain property which LBIE holds or controls and which belongs to its customers”. The proposal goes on to explain that as part of its business LBIE “held, directly or indirectly, significant quantities of assets in trust for its customers” and that “[w]here assets are held in trust, they do not form part of LBIE’s general estate but instead are held by LBIE as trustee for the benefit of those persons who have claims to those assets”.

5. The question of jurisdiction which has been debated is whether it is possible to resort to a scheme of arrangement with creditors under Part 26 of the 2006 Act for the purpose identified in the proposal. It raises the question whether what is proposed is a “compromise or arrangement” within the meaning of section 895 of the 2006 Act.

The background

6. In a witness statement made in support of this application, David Ereira, a partner of Linklaters, sets out what has led to the proposal. He explains that one of LBIE’s major business areas has been that of prime services where LBIE acted as prime broker to institutional clients, mostly hedge funds. He goes on to explain that, as prime broker, LBIE provided a broad range of services, including execution of securities and derivatives trades, clearing and settlements of trades (whether executed by LBIE or by other executing brokers on its behalf), custody, financing, foreign exchange, stocklending, and valuation and reporting for the client’s portfolio. LBIE’s clients, he states, would often actively trade in securities and derivatives, taking both long and short positions, and would also require stock borrowing and financing facilities and foreign exchange services. LBIE’s prime services clients comprised the majority of entities which, as the result of the various contractual arrangements which he later describes, have proprietary interests in assets held by or on behalf of LBIE. Other persons with such interests included clients who placed securities with LBIE by way of safe custody, private individuals whose accounts were dealt with by the Private Investment Management division of LBIE, market counterparties who posted collateral with LBIE pursuant to derivatives trades otherwise than on a title transfer basis and LBIE’s affiliates within the Lehman group of companies.
7. LBIE did not hold assets itself but did so through depositories, exchanges, clearing systems and sub-custodians. The method used depended on the type of assets held, the systems through which assets were traded, the currencies involved and regulatory requirements.
8. Mr Ereira summarises the principal contracts entered into by LBIE where the clients and counterparties retained a proprietary interest in assets transferred to LBIE. They are International Prime Brokerage Agreements, Master Custody Agreements, Margin Lending Agreements, and what is described as the Credit Support Annex (New York law version) to the ISDA Master Agreement. Mr Ereira also refers to LBIE’s standard terms of business which set out the terms on which LBIE might hold assets for the client. He points out, however, that his understanding was that when holding assets for a client LBIE would normally have entered into one or more of the other contracts the terms of which would prevail over LBIE’s standard terms of business in the event of any inconsistency.

9. Mr Ereira then embarks upon a review of some of the key terms of LBIE's standard terms of business and of the principal forms of contract which LBIE entered into where clients retained a proprietary interest in assets transferred to LBIE, pointing out, however, that his review was by reference to what he describes as the "pro-formas" or standard terms in use at the time LBIE went into administration or versions which were regularly entered into by LBIE. He explains that the agreements were usually subject to some degree of negotiation with the client.
10. I do not think that any useful purpose will be served in seeking to summarise how these various contracts operate. A key consideration in respect of any client, once the contractual terms governing that client's relationship with LBIE have been established, is to identify what, as at the date that LBIE went into administration or later in the case of financial contracts which were still open at that time, the net financial position is as between LBIE and the client and, in particular, whether there is a net sum due from the client to LBIE or vice versa. A no less important consideration is to identify what rights, if any, LBIE is entitled to exercise over assets of the client held or controlled by LBIE in the case where there is a balance due from the client to LBIE, either generally or in respect of any particular transaction or series of transactions. I do no more than summarise the issues.
11. Those questions aside - the net financial position between LBIE and the client and the extent to which LBIE is entitled to have recourse to a client's assets to satisfy LBIE's monetary claim or claims against that client - the administrators have faced a range of complex issues in seeking to give effect to a client's entitlement to the return of its assets. Those difficulties are described thus in Mr Ereira's witness statement:

"...the most fundamental of the obstacles which they [the administrators] face is the fact that, as matters currently stand, they cannot be certain who is entitled to the Trust Property. Distributing assets in such circumstances potentially gives rise to claims against LBIE for breach of trust and to related claims against the Administrators. Likewise clients to whom Trust Property is distributed cannot be certain that they will not face proprietary claims from other clients in respect of such Trust Property ..."

The expression "Trust Property" has a particular meaning under the scheme. For present purposes it refers to assets held in trust for the client. The problems faced by the administrators, and the reason why they seek to overcome them by means of a scheme of arrangement containing a "bar date" for claims (as it is described) is, in summary, because (1) they have not received responses from all clients to the enquiries that have been made, (2) they cannot rely upon the accuracy of LBIE's books and records and (3) they have likewise not received all the information requested of custodians, depositories and affiliates as regards assets held on behalf of LBIE.

12. Mr Ereira then goes on to describe how the administrators have written to 1,707 account holders thought potentially to have claims against LBIE for the return, or in respect, of such assets in order to obtain from them full details of the claims, rights or other interests which the clients purport to have in relation to such assets. The information sought has included confirmation of positions and balances held with

LBIE as at the time on 15 September 2008 when LBIE was placed into administration, copies of any contractual agreements and other relevant documentation and details of all positions terminated or closed since that time, together with the basis of any valuations assumed in the client's calculations. In addition, as Mr Ereira explains, the administrators have issued a notice on the administration website inviting those clients and counterparties to whom such letters were not sent but who nonetheless believe that they might have such interests, to supply details of what claims, rights or interests they believe that they might have in relation to any client assets. He reports that as at 29 May 2009 the administrators had received 950 responses to the letters and notices and that the overall number of trust property claims received was 1,214 of which over 120 were considered as "potential priority claims" by a committee set up by the administrators to apply and keep under review certain prioritisation principles referred to in the schedule to an order which the court made on 7 October 2008.

13. Mr Ereira states that the scheme "would provide certainty as regards the pool of persons to whom Trust Property could potentially be distributed" and "would also ensure finality (as between LBIE and any given Scheme Creditor and as between Scheme Creditors) as regards the Scheme Creditors' entitlements to Trust Property distributed to them under the Scheme". He goes on to say that without the scheme "it may not be possible for the Administrators to identify with certainty the persons to whom Trust Property should be returned" and that without that certainty "it will not be possible to distribute Trust Property on a basis that provides finality for the recipients and avoids exposing LBIE and the Administrators to potential claims".
14. Mr Ereira then explains that in addition to the difficulty in returning client assets to clients, the administrators face other complex issues regarding the return of such property. For example, they have to determine how any shortfalls in assets are to be shared between clients, determine the terms of a client's contract where there is a lack of documentation, find a way of terminating open contracts in order to crystallise a client's overall financial position with LBIE, determine how set-off is to apply in any given case and agree valuations for derivatives and other complex financial transactions. These, it seems, are relevant to the rights of retention/security available to LBIE under the contractual arrangements entered into with clients. A scheme, he explains, would not only provide certainty as regards the persons entitled to client assets, but would seek to deal with those and other issues which would otherwise complicate the return of such assets.
15. In a section headed "How claims have been dealt with to date" Mr Ereira sets out the practical difficulties which the administrators have faced in those cases where assets have been returned to clients on a prioritised basis. In order to safeguard against the risk that it might later be determined that the assets in question should not have been returned because, for example, they are the subject of competing claims, the administrators have required the receiving clients to enter into a deed providing for the return of the assets (or such portion of them as may be appropriate or their value) to the extent that it might be established that the assets should not have been returned together, where appropriate, with credit support and costs. The arrangements are explained at greater length in paragraph 70 of Mr Ereira's statement.
16. The administrators recognise that this is an unsatisfactory way of approaching matters and does not meet clients' needs. For example, it does not provide finality in that

clients who accept the return of assets on this basis remain liable under their undertaking to return. Moreover, the clients may experience difficulty in providing credit support for their undertakings. Over and above these and similar problems, the process is time-consuming and costly. Mr Ereira reports, for example, that as at July there are 165 accounts where the administrators are in a position to return assets but where many of the clients in question are either unable or unwilling to comply with the administrators' terms for distribution.

17. It is in order to address these difficulties and facilitate the return of assets that the administrators have concluded that it is expedient to promote a scheme of arrangement. In formulating the scheme they have set up a working group to act as a "sounding board" for discussion of the scheme and its terms. The group consists of representatives of the administrators, personnel from Linklaters (including Mr Ereira himself) and the creditors' committee members, including an unsecured creditor who will not qualify as a scheme creditor under the scheme as well as creditors who will qualify as scheme creditors. One of the members is Lehman Brothers Holdings Inc., the overall holding company in the Lehman group. It has written to the court to commend the scheme (as have two other members of the group). Two industry bodies, the Alternative Investment Management Association and the Managed Funds Association have also been consulted. All of this has resulted in a continuing process of discussion on the structure and content of the proposed scheme.
18. The administrators accept that, in the event that the proposed scheme is not implemented, they will have no option but to continue with their current approach to establishing creditors' entitlements to and the distribution of client assets. They state that failing such a scheme the resolution of many of the uncertainties which they face in reconciling client positions would be, in the words of Mr Ereira, "extremely problematic". To do so, he continues, "would likely require either the promulgation of an alternative scheme of arrangement (which would involve further significant delay), or numerous further applications to the Court for directions". Uncertainties with respect to possible competing claims would be likely to cause them to continue to require significant indemnities backed by credit support as a condition of asset distribution.
19. Mr Ereira states that the administrators are aware of the fact that their actions in respect of the return of client assets "will be the subject of considerable interest both in the UK and abroad and that comparisons may well be sought to be drawn between the insolvency regime prevailing in England and Wales and that in other jurisdictions where the Lehman Brothers group did business prior to its collapse". He concludes by saying that the administrators "consider that the proposed scheme offers Scheme Creditors a flexible and bespoke process for facilitating the prompt return of Trust Property and thus has the potential to demonstrate the efficacy of the insolvency regime in this jurisdiction".
20. Thus the scheme is presented as, virtually, a practical necessity and as a demonstration of the ability of the insolvency process in this jurisdiction to respond to the challenges presented by this most complex of administrations.

The proposed scheme

21. Although very detailed in its terms, it is not necessary to set out the proposed scheme at any length. It is sufficient to draw attention to certain of its key provisions.
22. The scheme is intended to deal with persons who are described as “Scheme Creditors”. These are persons who have claims against LBIE at the time it was placed in administration (the “Time of Administration”) for or in respect of what are described as “Segregated Assets”. The claims must be capable of being satisfied by the delivery, in whole or in part, of the Segregated Assets. Segregated Assets are defined as “any Security which at the Time of Administration was held on a segregated basis” meaning that the asset “was recorded as being held separately from LBIE’s own Securities in both the Books and Records of LBIE and also at LBIE’s custodian or depository (the Intermediary)...” “Security” is defined as any financial instrument, including any share, instrument creating or acknowledging indebtedness, instrument creating or acknowledging entitlements to investments, warrant and unit in a collective investment scheme...” It excludes money. I was told that there are approximately 28,000 different categories of security to be dealt with.
23. A Scheme Creditor is expressly described as excluding anyone whose claims “are not proprietary but are only unsecured”. Equally, as Mr Trower explained in the course of argument, a Scheme Creditor will not include anyone who has no kind of pecuniary claim, however contingent, against LBIE. Thus, a client with a claim to a particular security but who renounces any pecuniary claim (for example, for damages for late delivery of the security) and confines his claim to its return will not be included. In short, a person is only a Scheme Creditor if that person (1) has a pecuniary claim against LBIE and (2) has a proprietary claim to a security which was held on a segregated basis at the Time of Administration.
24. The scheme explains, in what is described as “Key Concept 2”, that “the subject matter of the Scheme is Trust Property”. Trust Property is wider than “Segregated Assets” because it includes assets, referred to as “Derived Assets”, which are derived from Segregated Assets, and “Recovered Assets”. Recovered Assets are assets received by LBIE from a source which has an obligation to redeliver to LBIE a security which had been delivered by LBIE to that source after the Time of Administration but prior to the date (“the Effective Date”) when a copy of the court’s order sanctioning the scheme under Part 26 (assuming such an order is made) is delivered to the Registrar of Companies.
25. The scheme is intended to deal with all of a Scheme Creditor’s proprietary claims against LBIE for the return of Trust Property. It extends to property which LBIE should have held even if in fact it does not. This is subject only to the requirement that LBIE must hold some property of the Scheme Creditor and means therefore that if the claim is confined to an unsecured pecuniary claim against LBIE, the claim will not be dealt with under the scheme.
26. The key provision of the scheme, set out in Part 2 of Section 4 of the proposal, is that Scheme Creditors release all claims (save for certain “Excluded Claims”) against LBIE, the scheme supervisors, the administrators and other Scheme Creditors, including all claims for or in respect of (1) any “Asset Claim” (meaning, put shortly, a claim against LBIE in respect of any Trust Property), (2) any payment for or on

account of any asset which is or was at any time the subject of an Asset Claim, (3) damages, indemnity or contribution in respect of any loss, cost or expense in connection with any asset which is or was at any time the subject of an Asset Claim, (4) all liabilities for breach of contract, loss or damage, indemnity or contribution of any nature, (5) all rights to seek or enforce judgment, exercise any remedy or apply any set-off, netting, withholding, combination of accounts or retention or similar rights against LBIE in respect of any claim or liability, and (6) all rights in respect of any financial contract. These are defined as “Released Claims”.

27. In exchange for their Released Claims, Scheme Creditors are given what are described as “New Claims”. Broadly stated, these are (1) the right of each creditor to have its net contractual position (as earlier summarised) and what are described as “Allocations and Distributions” determined on the basis set out in the Scheme, (2) the right to have such part of the Trust Property as is available for distribution under the scheme allocated to and then delivered to the creditor, alternatively appropriated by LBIE in or towards discharge of the creditor’s liabilities to LBIE (or certain affiliates or other third parties), (3) the right to claim against LBIE in accordance with the scheme for the amount of that creditor’s net contractual position (assuming that the position has resulted in an amount owing by LBIE to that creditor) as a new obligation of LBIE and (4) the right to claim in LBIE’s winding-up or any other distribution of LBIE’s assets for such amount as is determined under the scheme. The New Claims are subject to an overriding proviso that no Scheme Creditor is entitled to recover more than once in respect of the same asset or claim.
28. The reference to “Allocations” is, shortly stated, to the right of LBIE to allocate Trust Property available for distribution under the scheme to a Scheme Creditor by reference to individual stock lines (for example the quantity of a particular quoted security) held as Trust Property. Paragraph 10.7 of “Key Concept 6” (concerned with “Allocations and shortfalls”) provides in terms that “a Scheme Creditor’s entitlement to participate in an Allocation will be based on its Asset Claim”. This in turn is to be determined by LBIE based on certain information available to it. The Scheme Creditor has the opportunity to challenge the determination through a dispute resolution mechanism. Paragraph 10.8 requires the Scheme Creditor when receiving anything in respect of its Asset Claim to account for any assets received from an Intermediary (rather than from LBIE direct) and paragraph 10.10 provides, in effect, that if the allocations made to a Scheme Creditor result in a shortfall then the value of that shortfall is to rank as an unsecured claim against LBIE.
29. The broad effect, although the drafting of the scheme is a little dense at this point, is that, subject to certain exceptions, LBIE will match a Scheme Creditor to a particular stock line where LBIE can be satisfied on the information available to it that the creditor has a proprietary claim (the so-called “Asset Claim”) to assets answering the description of that stock line. This is on the basis that the creditor’s claim will be satisfied (by means of the “Distribution”) out of that stock line so far as is possible having regard (1) to the overall quantity of the stock line available for distribution and (2) to the competing claims of other creditors to the same stock line.
30. But there is an important qualification to this which is set out in Part 3 of Section 4. This is the provision of a cut-off date (the “Bar Date”) for the submission of claims under the scheme. The date envisaged is either 31 December 2009 or, if later, the last business day of the second full calendar month following the Effective Date.

Paragraph 21.1 provides that “[a]ny claim submitted after the Bar Date can be disregarded by LBIE”. But this is subject to an exception: if by the Bar Date a Scheme Creditor has failed to submit a claim (by completing a pro forma claim form) LBIE will calculate that Scheme Creditor’s entitlement under the scheme using “Relevant Information”. This is information capable of ascertainment from LBIE’s books and records, information contained in the Scheme Creditor’s claim form (if one has been submitted) and also, shortly stated, information from various notices delivered under the scheme as well as information made available by intermediaries, affiliates and any relevant exchange. Once the Bar Date has passed LBIE will start allocating, appropriating and distributing on the basis of pre-Bar Date claim forms and other Relevant Information. This means that if a Secured Creditor fails to submit a claim form by the Bar Date and, by that date, LBIE is without any Relevant Information in relation to that Scheme Creditor’s claim, the claim may be disregarded.

31. However, as Mr Trower explained in the course of argument, the imposition of a Bar Date is not intended to have the consequence that the late claim is altogether barred. If the Scheme Creditor can substantiate its claim, then, notwithstanding that this is after the Bar Date, it may share in the particular stock line, but it may only do so if and to the extent that there is any surplus in that stock line. Thus, if there are no other claimants to a particular stock line (or the claims of those other claimants have been fully satisfied), the late claimant is unaffected by the Bar Date. Conversely, if there is insufficient in the stock line to satisfy the accepted claims of pre-Bar Date claimants, the later claimant will be left to claim as an unsecured creditor. In short, there is no “catch-up” concept for late claimants as regards any distribution: they must await the full satisfaction of the accepted claims of pre-Bar Date established claims.
32. For present purposes, the scheme may be summarised by saying that a client of LBIE who qualifies as a Scheme Creditor - in that the client has, or potentially has, a pecuniary claim against LBIE and is the owner of a particular asset held or controlled by LBIE (for example a quantity of a particular quoted security) - will have that asset claim satisfied on a pooled basis, ranking alongside (and in competition with) others who can establish ownership claims to the same asset, to the extent that the securities comprising that asset are available to meet the claims. The unrecovered value of the client’s Asset Claims and any balance due to the client on computing the client’s net contractual position with LBIE resulting from the closing out of all financial contracts between the client and LBIE are to rank as unsecured claims against LBIE. All other pecuniary claims of the client against LBIE are foregone.

The effect of the scheme

33. There is no doubting - indeed Mr Trower freely accepted - that, as so drawn, the scheme will interfere with the client’s property rights in assets held for that client on a fiduciary basis by LBIE and that this may happen against the will of that client. For it is of the essence of a scheme under Part 26 that this may occur precisely because a majority in number representing 75% in value of the creditors or class of creditors can enforce its will on the dissentient minority subject only to the correct identification of the relevant class (or classes) and to obtaining the court’s sanction to the arrangement which the majority has approved.
34. That the scheme will interfere with a client’s property rights is evident in at least three respects. First, it does so by providing in terms that Scheme Creditors release all

asset claims in exchange for “New Claims”. It is irrelevant, therefore, that a particular batch of securities can be identified as having come from a particular client and that the batch is sufficient to meet that client’s claim in full; if there are other securities of the same stock line, all are grouped together to constitute the pool out of which Scheme Creditors who have ownership claims to securities of that kind must share; if overall there is a shortfall, the Scheme Creditors in question share that shortfall rateably. (In fact, the scheme provides for three pools of securities – see paragraph 10.3 – but the principle of rateable sharing in the event of a shortfall applies to each pool.) Second, the client who fails to submit its claim by the Bar Date - and in respect of whom LBIE has no “Relevant Information” - stands to lose its asset altogether; its only hope of recovery is from any surplus available after the claims to that stock line by the other (pre-Bar Date) claimants have been fully satisfied. Third, the Scheme Creditor will only recover any assets by way of distribution under the scheme by undertaking a series of warranties set out in paragraph 27 of Part 4.

35. The question is whether a scheme to distribute client assets held by a company such as LBIE under which LBIE is empowered to interfere with the client’s property rights (and do so without that client’s consent) is one which is within the scope of Part 26.

Counsel’s submissions

(a) The administrators

36. Mr Trower submitted that the scheme seeks to replace Scheme Creditors’ existing rights against LBIE (and against other released parties) with new rights. It does so for two reasons. First, it does so to put in place systematic procedures to facilitate the return to clients of Trust Property. Second, it does so to crystallise the Scheme Creditors’ net contractual positions with a view to dividends being paid to them in due course in respect of any unsecured claims that they may have against LBIE’s estate after the application of LBIE’s security rights, set-off rights and other deductions.
37. Under the scheme, properly understood, LBIE will return assets to those clients who are entitled to them, but where LBIE does not have enough of a certain security to meet the proprietary claims of the creditors in respect of that security, the scheme provides for them to share the burden of the shortfall equally. The intended result will be that each client receives its share of the relevant Trust Property which is available to be distributed (taking into account shortfalls, set-offs and third party security rights over the assets) and the determination of any net unsecured claims it has against LBIE. Although, as a matter of form, the scheme refers to the “release” of the client’s rights against LBIE in favour of “new claims”, it does not set out to vary, much less extinguish, clients’ property rights. Rather, it varies the contractual relationships between creditors and LBIE, and in particular the underlying contractual claims, with a view to facilitating LBIE’s ability to give effect to existing proprietary rights so far as it is possible to do so. It is concerned therefore to vindicate the clients’ property rights.
38. The key questions to be considered are two-fold. First, are the Scheme Creditors creditors of LBIE? Second, is what is proposed a compromise or arrangement between LBIE and those creditors? Mr Trower submitted that both questions were properly to be answered into the affirmative.

39. The scheme, he pointed out, is confined to those with pecuniary claims against LBIE. Giving the word “creditors” appearing in section 895 its full width (in accordance with *Re T & N Ltd* [2005] EWHC 2870 (Ch); [2006] 1WLR 1728), namely anyone with a pecuniary claim, whether actual or contingent, against the company arising out of some obligation entered into with, or imposed by law on, a company, it is likely that all, or just about all, clients owning property which LBIE holds or controls will have a pecuniary claim against LBIE and thus be a creditor of it. It is correct therefore that clients with such claims are described in the scheme as “Scheme Creditors”. The fact that it may be difficult accurately to estimate the value of the claim or contingency does not mean that the person is not a creditor. The claims extend to actual or contingent claims for breach of trust by LBIE; the fact that the parties are also in the relationship of trustee and beneficiary does not mean that they cannot also be debtor and creditor in respect of each other.
40. Equally irrelevant to the creditor’s status as a creditor for the purpose of section 895 is the fact that the creditor’s claim is secured on the company’s property or that, under a scheme of arrangement, the creditor may be deprived of its security. This was established in *Re Empire Mining Company* (1890) 44 ChD 402 (North J) and *Re Alabama, New Orleans Texas and Pacific Junction Railway Company* [1891] 1Ch 213 (North J and the Court of Appeal) where the relevant provisions (the statutory predecessors of Part 26) were sections 2 and 3 of the Joint Stock Companies Arrangement Act 1870. In *Alabama* Lindley LJ stated (at page 236) that:

“It is in those cases the Legislature has thought fit to enlarge the power of making compromises or arrangements, and the language of the section [section 2] is wide enough to include all creditors, whether they hold securities or whether they do not hold securities - they are still creditors; and they can come in if they like and prove. If they are amply secured they need not come - they can hold their securities; but still they are creditors.”

In the same case Fry LJ referred to the jurisdiction conferred by the 1870 Act as being “of the largest description” and stated that “to exclude from the arrangements or compromises to be made an arrangement or compromise which affected the security ... [would] be putting a most unwarrantable restriction on the generality of the language used in the Act...”

41. Mr Trower submitted that the court frequently sanctions schemes of arrangement affecting the property rights of creditors over assets which secure the company’s indebtedness to them, for example where, as in *Empire Mining*, the scheme involves a debt for equity swap the effect of which is that lenders holding security over the company’s assets release the company from its indebtedness to them - and release the security held by them (or on their behalf) - and do so for an equity stake in the scheme company. The company is thereby freed from the security structure previously in place.
42. In the case of LBIE, the persons who are to be bound by the scheme as Scheme Creditors are all creditors, actual or contingent, of LBIE. At the very least they have claims arising out of the fact that they have been kept out of their property since LBIE went into administration. The evidence shows that many of them have demanded

back, but have not yet recovered, their property after LBIE went into administration. This failure to return is not something which the administrators have engineered. It is a consequence of the complexity of LBIE's financial affairs that has confronted the administrators.

43. Like the word "creditors", the words "compromise" and "arrangement", as appearing in section 895, are to be afforded a wide construction. Parliament has not sought to define them, and the courts have been unwilling to do so either. In *Re T & N Ltd (No.3)* [2006] EWHC 1447 (Ch); [2007] 1 BCLC 563, David Richards J summarised (at [50]) the effect of the authorities on the scope of those expressions when he said:

"A scheme of arrangement which did no more than expropriate the interest of a member or creditor would not be a compromise or arrangement within s425 (see *Re NFU Development Trust Ltd* [1973] 1AER 135, [1972] 1 WLR 1548). Brightman J observed that a compromise implies some element of accommodation on each side and that an arrangement implies some element of give and take. Total surrender or confiscation was not within either of them. In commenting on this decision in *Re Savoy Hotel Ltd* Nourse J said ([1981] 3 AER 646 at 652, [1981] Ch 351 at 359) that the word 'arrangement' in s425 and its predecessors is one of very wide import, a proposition which was by no means diminished by Brightman J's judgment: 'all that that case shows is that there must be some element of give and take. Beyond that it is neither necessary nor desirable to attempt a definition of "arrangement".' As members' schemes such as that in *Re Savoy Hotel Ltd* show, the give and take need not be between the members and the company, but may be between the members and a third party purchaser, with the company's only function being to register the transfer of shares and thereby terminate the existing members' status as members."

44. Mr Trower submitted that *Re T & N Ltd (No.3)* itself illustrates the width of meaning which the court is willing to accord to an arrangement. David Richards J stated (at [53]) that:

"...it is not a necessary element of an arrangement for the purposes of s425 that it should alter the rights existing between the company and the creditors or members with whom it is made. No doubt in most cases it will alter these rights. But, provided that the context and content of the scheme are such as properly to constitute an arrangement between the company and the members or creditors concerned, it will fall within s425. It is, as Nourse J observed, neither necessary nor desirable to attempt a definition of arrangement. The legislature has not done so. To insist on an alteration of rights, or a termination of rights as in the case of schemes to effect takeovers or mergers, is to impose a restriction which is neither warranted by the statutory language nor justified by the courts' approach over many years to give the term its widest meaning.

Nor is an arrangement necessarily outside the section because its effect is to alter the rights of creditors against another party or because such alteration could be achieved by a scheme of arrangement with that other party.”

45. Another and important indication of the wide scope of the expression “arrangement” is the willingness of the courts to sanction schemes affecting creditors’ proprietary rights in respect of the security granted to them by the relevant company. In those cases, the arrangement of rights and obligations affects not just the creditor’s ability to pursue its *in personam* claim against the company *qua* creditor, but also the creditor’s ability to exercise its separate proprietary rights.
46. Mr Trower summarised the position by submitting that if it is possible to link the right which is sought to be rearranged by the scheme (for example, the proprietary claims of a secured creditor) to the claim which that creditor has against the company *qua* creditor, the scheme is capable of being an arrangement. Thus, the fact that the scheme seeks to affect a proprietary right which a creditor may be able to pursue quite independently of the rights which he has *qua* creditor, for example, to prove in a winding-up, does not mean that it cannot be an arrangement. From that position, he went on to submit that once it is established that a scheme under Part 26 is capable of affecting proprietary (and indeed other) rights which a creditor may have, there is no reason in principle why such a scheme should not be capable of affecting all types of proprietary right, so long as it is entered into with persons who are, in fact, creditors and so long as the variations for which it provides do at least “concern” their position as creditors. In particular, he said, there is no reason in principle why any other proprietary claim which a person who is a creditor may have should be treated any differently from a proprietary right granted as security for indebtedness.
47. He submitted that the issue of principle raised by the administrators’ application is simply whether the variation which the scheme would impose on Scheme Creditors’ rights, as beneficiaries of trust property held by or to the order of LBIE, are such that it can no longer be said that the scheme as a whole is made with them in their capacity as creditors of LBIE and that it or some part of it does not concern their claims as such. From the perspective of the administrators and LBIE, the essence of the scheme is the need to ensure that, in returning assets to those entitled to them, the administrators do not expose LBIE or themselves to claims for breach of contract, trust or duty. It is the capacity of the Scheme Creditors as creditors with actual or contingent claims against the Released Parties which underpins the need for the scheme. Any such claims against LBIE would be personal claims for breach of contract and/or trust. The question of capacity is the capacity in which the Scheme Creditors have claims against LBIE arising out of LBIE’s failure to comply with its contractual obligations in respect of, and to return, Trust Property. It is difficult to see why the fact that the scheme may affect their ability to enforce their proprietary rights against LBIE and other Scheme Creditors would of itself mean that the arrangement does not “concern” them as creditors.

(b) GLG Partners LLP

48. Mr Zacaroli said that GLG Partners LLP strongly supported the broad principles of the scheme. It therefore supported the administrators’ application. He noted that the scheme working group included both clients, such as his own, which had property

rights that would be affected by the scheme and also, as a balancing factor, a purely unsecured creditor. He emphasised the commercially desirable objective of the scheme of releasing, far earlier than would otherwise be the case, the billions of dollars of securities effectively trapped in LBIE since the administration started. He pointed to the complexity of the relationships between LBIE and the majority of its clients where, as he put it, the resolution of clients' personal (non-proprietary) claims is inextricably linked with their proprietary claims in that establishing the existence and extent of the former is likely to have an impact on the asset distribution entitlement both of that client and of others. He submitted that it was wrong to focus on the variation or extinction of existing property rights and that, in truth, such variations as are proposed to existing property rights are part and parcel of a wider scheme intended to resolve the overall position between Scheme Creditors and LBIE and are included for the purpose of ensuring that the property rights are given effect to as far as possible. He submitted that the words "creditor" and "arrangement" appearing in section 895 were to be construed broadly and that just as a scheme may validly affect rights between creditors and third parties (as *Re T & N Ltd (No 3)* shows) so also may a scheme validly affect a person's property rights.

(3) LIBA

49. Mr Snowden submitted that the central purpose of the proposed scheme is to vary and, in some cases, extinguish altogether the proprietary rights of owners in respect of assets held on trust by LBIE and to do so not because the owner consents but because others owning property under other trusts who happen to share the same corporate trustee, LBIE, agree by the requisite majorities under Part 26 to do so. The fundamental right of a property owner, however, is to exclude anyone else from enjoyment of his asset and, where the property is held on trust, to have that trust administered according to its terms and the general law. See *Target Holdings Ltd v Redferns* [1996] 1AC 421 at 434A (Lord Browne-Wilkinson). Even where, under the terms of more sophisticated trusts, the assets due to several beneficial owners are lawfully pooled, each beneficial owner still has specific property rights in respect of a specific fund of assets. Those rights are not the rights of a creditor and they cannot be varied save with the beneficial owner's consent, or under the terms of the relevant trusts themselves, or in the very limited circumstances permitted by the Variation of Trusts Act 1958.
50. LIBA's core objection to the scheme is that, even if it is confined to clients who have both proprietary rights to assets held by LBIE and pecuniary claims against LBIE, it purports to extinguish both the proprietary rights and the pecuniary claims of those customers and to replace them with rights (the "New Claim") under the scheme. The extinction of property rights and their replacement with rights under the scheme is not a compromise or arrangement made with a client in his capacity as a creditor, and to that extent it falls outside the jurisdiction of the court under Part 26.
51. On analysis Part 26 is concerned with the general estate of a company. It cannot override ordinary trust principles. In the case of creditors, whether actual, prospective or contingent, it deals with persons who have claims which they can bring against the pool of assets which comprises the general estate of the company. A creditor's claim ranks *pari passu* with other creditors' claims against that general estate. It is perfectly comprehensible, therefore, that Part 26 should provide that if those creditors wish to rearrange or compromise their rights against the company,

they should be able to do so, by the requisite majorities, because, at the end of the day, they all look to the company's assets for satisfaction of their pecuniary rights.

52. By contrast with that is the person who has placed his assets with a trustee. There the position is totally different: the essential feature of so doing is that the owner knows that he can have his property, which remains his throughout, dealt with by the trustee in accordance with the terms of the trust. The property is not vulnerable to interference merely because the trustee becomes insolvent: the trust remains. The fact that the trustee is a corporate trustee is likewise immaterial to the integrity of the trust; no less immaterial is that the trustee happens to be a company liable to be wound up under the Insolvency Act 1986 (or the equivalent provision in Northern Ireland), these being the types of company to which the court's jurisdiction under Part 26 applies where a compromise or arrangement is proposed between a company and its creditors or any class of them: see section 895(2)(b).
53. The fact that the proposed scheme is confined to persons who have a pecuniary claim, however prospective or contingent that claim may be (for example a claim for damages or compensation for the delay in returning that person's property), does not assist the administrators. While the existence of that claim may provide the basis for a scheme of arrangement directed to that and other pecuniary claims against LBIE, it does not justify interference with the underlying property rights of the property owner. Aside from the fact that the property owner's remedy (as beneficiary under the trust) for breach of trust is principally directed to securing performance of the trust, rather than to the recovery of compensation or damages, the existence of the pecuniary claims does not affect, and is certainly not the origin of, the owner's property rights. To suggest otherwise and to ground the intention of the scheme to interfere with the owner's property rights merely because that owner also has a pecuniary claim against LBIE in view of the possibility that LBIE has acted (or may yet act) in breach of trust is to invert the position. Indeed, the scheme, if it is allowed to proceed, risks turning the position of the beneficial owner on its head: this is because under a trust it is for the trustee to justify and account for his dealings with the trust estate whereas under the scheme the onus will be on the owner to come forward, as a dissentient, to explain and justify why that owner's property rights should not be dealt with and varied under the scheme.
54. Mr Snowden went on to submit that there is no justification in the authorities for the approach which LBIE wishes to adopt. The security cases (*Empire Mining* and *Alabama*) do not assist the administrators' arguments for two reasons. First, all that happened in those cases was that the underlying debt was schemed away: this had the consequence that there was nothing left for the security to secure. In effect, the security was released. This is conceptually different to altering the client's property rights without, or without necessarily, affecting the creditor's pecuniary claims against LBIE. Indeed, on analysis, the existence of a pecuniary claim serves as no more than a pretext or peg on which to mount the scheme which is designed to interfere with property rights. This can be seen from the fact that any shortfall in available assets to meet the client's property entitlement (described in the scheme as an "asset shortfall claim") - the very existence of which has caused the client to be treated as a Scheme Creditor - survives in full as an unsecured claim against LBIE. (See paragraph 10.10 of the scheme.) This can also be seen from the fact that the only reason why some at least of LBIE's clients are Scheme Creditors within the

purview of the scheme is because subsequent to the Time of Administration LBIE failed to return trust assets to their owners. It thus appears that LBIE is praying in aid its own failure or refusal, after the making of the administration order, to return trust assets as a means of bringing those persons within the scope of Part 26 in order to interfere with their property rights. In any event, a secured creditor is someone who has managed to negotiate with the company that some or all of the company's assets are appropriated specifically to answer his pecuniary claims. Subject to satisfaction of those claims and any secured claims ranking after them, the assets are available to meet the claims of the company's unsecured creditors. To that extent, the secured creditor has lifted himself up in the queue for the distribution of the company's assets. It is comprehensible therefore that Part 26 should permit people in that position to reorganise their claims (as such a group) against the company. That is fundamentally different to the case where the property in question is not that of the company but property which is, and at all material times has been, exclusively that of the company's client.

55. The administrators' reliance on in *Re T & N Ltd* is likewise misplaced. In that case David Richards J (at [40]) emphasised that the mechanism under section 425 (the predecessor to sections 895 and following) whereby an arrangement may be imposed on dissenting or non-participating members of the class "is not to be construed as extending so as to bind persons who cannot properly be described as creditors". In *Re T & N Ltd (No 3)* the same judge (at [45]) stated that in any compromise or arrangement (whatever the precise meaning of those expressions) with creditors or members of a company:

"[i]t is implicit that it must be made with them in their capacity as creditors or members and that it must at least concern their position as creditors or members of the company."

David Richards J plainly did not consider that the requirement in Part 26 that a compromise or arrangement be between a company and its creditors should serve as no more than a gateway, enabling the court to sanction a substantive interference with the rights of persons who happen to be creditors but where the rights in question were held in a different capacity.

Conclusions

56. At the heart of this debate is a simple question: is there jurisdiction under Part 26 to sanction a scheme, so that it becomes binding on dissentients, which has as its purpose the distribution of property held by a company on trust? For that, in essence, is what the scheme is about.
57. The key question to my mind is whether the scheme proposed affects the clients who are intended to be bound by it in their capacity as creditors of LBIE. Insofar as it does not, there is, in my judgment, no jurisdiction under Part 26 to force the scheme on those clients who do not assent to it.
58. In my judgment, it is abundantly clear that the scheme is largely concerned with the discharge by LBIE towards its clients of its obligations concerned with the holding or control of client property, in particular the return of that property to the clients for

whom it is held. As such and largely for the reasons advanced in argument by Mr Snowden, it is outside the scope of Part 26.

59. It is nothing to the point that LBIE's concern is to vindicate clients' property rights or to facilitate the early return of the property in question, highly desirable though those aims obviously are. The fact that the clients may also have pecuniary claims against LBIE and, as such, are creditors (whether actual or contingent) of LBIE and that the claims stem from LBIE's conduct of their property rights is, to my mind, immaterial. The fact that the ascertainment of clients' net contractual positions is intimately linked to their claims as property owners, both as against LBIE and *inter se*, is likewise immaterial.
60. I can find nothing in *Re T & N Ltd (No 3)* which provides support for the administrators' contentions. In that case the schemes proposed were with the employees or former employees of companies who had or might in the future have claims for damages for personal injuries arising out of exposure to asbestos (and also with the dependants or relatives of such employees and with certain others). The claimants were collectively referred to as "EL claimants". The companies had, or thought they had, cover against such claims under policies of insurance ("EL policies") with certain insurers ("EL insurers"). The EL insurers asserted that the EL policies did not extend to asbestos-related claims or could be avoided on grounds of misrepresentation and non-disclosure. T & N sued the EL insurers to determine the extent of the cover provided by the EL policies. The EL insurers denied liability and claimed to avoid the EL policies. When the litigation had reached the Court of Appeal the proceedings were stayed for settlement discussions. These resulted in the negotiation of heads of agreement. The terms agreed involved a sum of £36.74 million being placed in escrow by the EL insurers. It was a term of the heads of agreement that schemes of arrangement should be entered into and sanctioned by the court in order to give effect to the proposals for the compromise and make them binding on persons who could claim under the EL policies. The essential features of the schemes were that, by way of compromise of the litigation, the scheme companies and the EL claimants would not assert claims against the EL insurers and that, instead, the sum placed in escrow would be held by trustees to pay a dividend on such claims as and when they were made and established. In particular, the schemes provided that all present and future rights of the EL claimants against the EL insurers and the fruits of any action to enforce such rights should be assigned absolutely to the trustees of the trust to be established pursuant to the schemes and that none of the EL claimants, the trustees or the scheme companies would be entitled to make any claim or assert any right against the EL insurers in respect of the EL policies or any EL claims.
61. The effect of the Third Parties (Rights Against Insurers) Act 1930 was that on entering administration the rights of T & N and the other companies under the EL policies in respect of liabilities incurred to EL claimants were transferred to those claimants whether or not they had yet made a claim. The underlying premise of the settlement and each associated scheme was that there was a genuine and substantial dispute concerning the validity of the EL policies and whether they covered asbestos-related claims.
62. Questions arose whether the scheme fell within section 425 of the 1985 Act as being a compromise or arrangement proposed between T & N and a class of its creditors. It was submitted that as the scheme did not purport to affect the rights between T & N

and its EL claimants it was not a compromise or arrangement between T & N and the EL claimants. In particular, it was submitted that the EL claimants' rights against T & N remained unaltered.

63. In his judgment David Richards J held (at para [45]) that:

“...whatever the precise meaning of a compromise or arrangement, it must be proposed with creditors or members of a company. It is implicit that it must be made with them in their capacity as creditors or members and that it must at least concern their position as creditors or members of the company.”

He concluded that even those claimants to whom T & N's rights against the EL insurers had been transferred by operation of the 1930 Act remained creditors of T & N. He considered that the word “arrangement” had a very broad meaning. He accepted that a scheme of arrangement which did no more than expropriate the interest of a member or creditor would not be a compromise or arrangement within section 425 and proceeded to make the comments which I have already set out at paragraph 43 above. He observed (at para [51]) that the rights of the EL claimants against the EL insurers compromised by the EL scheme were in no sense “unconnected” with T & N or the EL claimants' rights against T & N. He considered that the claims of the EL insurers to exclude asbestos-related disease from cover and to avoid the policies affected the position of both T & N and the EL claimants. He stated that if the EL claimants were unable to enforce their claims against the EL insurers, those claims would still lie against T & N, and that its assets (including any other available insurance cover) would be diminished accordingly. He considered that the litigation affecting the EL policies and its compromise therefore impacted directly on the EL insurers, T & N and the EL claimants alike.

64. Given those considerations, David Richard J reached the following conclusions:

“[52] The settlement of the litigation is therefore in substance and form a tripartite matter, involving T & N, insurers and claimants. That is reflected in the proposed scheme, with T & N and the claimants as parties and with the EL insurers appearing before the court to consent to the scheme and to undertake to be bound by its terms. It is true that the scheme has no effect on the present rights of EL claimants against T & N. The right of claimants to assert their claims against T & N, and the right of T & N to defend those claims, are unaffected, and claimants are not obliged to proceed first against the trust to be established by the scheme. However, if a claimant establishes a claim under the trust distribution procedures and receives a payment, it will diminish the amount which T & N would otherwise be required to pay in respect of the claim, if the EL insurers succeeded in avoiding the policies or in limiting the cover. Although not immediately affecting rights against T & N, the scheme is likely therefore to have an impact on those rights... The scheme of arrangement is an integral part of a single proposal affecting all the parties, which includes

also the trust and the trust distribution procedures to be established pursuant to the scheme.

[53] In my judgment it is not a necessary element of an arrangement for the purposes of s425 that it should alter the rights existing between the company and the creditors or members with whom it is made. No doubt in most cases it will alter those rights. But, provided that the context and content of the scheme are such as properly to constitute an arrangement between the company and the members or creditors concerned, it would fall within s425 ... To insist on an alteration of rights, or a termination of rights as in the case of schemes to effect takeovers or mergers, is to impose a restriction which is neither warranted by the statutory language nor justified by the courts' approach over many years to give the term its widest meaning. Nor is an arrangement necessarily outside the section because its effect is to alter the rights of creditors against another party or because such alterations would be achieved by a scheme of arrangement with that other party."

65. In my judgment, this case provides no support for the proposition that a scheme designed to deal with (and, so far as necessary, alter) the property rights of persons who happen also to be creditors of the scheme company constitutes a compromise or arrangement within the scope of Part 26. What clearly emerges from *T & N Ltd (No 3)* is that the scheme affected the EL claimants' rights against T & N as (and only as) creditors. It also, and directly, affected their rights against the EL insurers. But that was because the scheme was an integral part of a single tripartite proposal involving T & N, the EL insurers and EL claimants. Here, by contrast, the property rights of LBIE's clients - their Asset Claims in the terminology of the scheme - are enjoyed quite independently of any claims which those clients have against LBIE arising out of LBIE's defaults.
66. Mr Trower submitted that what mattered was whether the claims the clients had as creditors against LBIE "concerned" the claims that those clients had against LBIE in respect of their property held on trust by LBIE and that provided the one "concerned" the other, the sufficiency or closeness of the link was not a matter of jurisdiction but of discretion to be considered at the sanction stage of the proceedings. He relied on a passage from paragraph [54] of the judgment in *Re T & N Ltd (No 3)* in which David Richards J observed that "[t]he looser the connection between the subject matter of the scheme and the relationship between the company and creditors concerned, the more substantial might be the objections on discretionary grounds to sanctioning the scheme."
67. The question here, however, is one of jurisdiction not one of discretion. The observations of David Richards J assumed that the scheme affects the creditors as creditors.

68. What then of cases such as *Empire Trading* or *Alabama* where the courts said in terms that the word “creditors” (in what is now Part 26) can embrace creditors holding a security and where schemes were sanctioned notwithstanding that their effect was to deprive creditors of their security? The schemes in question were directed to the indebtedness owed to the debenture holders - the creditors - by the company in question. (In *Empire Trading* the arrangement gave to debenture holders fully paid-up shares in the company in lieu of their debentures and in *Alabama* the debentures were surrendered and replaced by new debentures.) But, as Mr Snowden pointed out, it was a consequence of the rearrangement of the company’s indebtedness that the debenture holders lost the benefit of their security: in effect there was no longer any indebtedness for the particular security to secure. Mr Snowden’s other point was that, in any event, the security comprised the particular company’s own assets. It is true that to the extent of the secured indebtedness the assets so charged ceased to be part of the company’s general estate. But, in such cases the company retains its equity of redemption in the assets in question. That right in the eyes of equity is no less than the continued ownership of the assets subject only to the particular charge. As such, it is property which it is open to the company to deal with like any other part of its assets. See *Buchler & anr v Talbot & ors* [2004] UKHL 9; [2004] 2AC 298 at [29] and also Snell’s Equity, 31st Edition at paras 37-01 and 27-02. In those circumstances, it is, as Mr Snowden submitted, entirely comprehensible that schemes under Part 26 concerned with the rearrangement of claims against a company’s general estate (which, on analysis, is the effect of any scheme by a company with its creditors) should be capable of extending to claims against the company secured on some or all of that estate.
69. In my judgment, the position is wholly different in the case of property which is not, and has never formed, part of the company’s assets and which the company holds as custodian or trustee (either directly or through others) for the clients as beneficial owners. In such a case, which is the position of clients who have entrusted property to LBIE, the obligation of LBIE is to administer the trust according to its terms, and to return the property to the client as beneficiary if that is what the client requests. Part 26 is simply not in point as a means of giving effect to the property rights of the client in question. If LBIE has any interest in the property at all, it is that of a creditor holding security (which may be no more than a lien) for indebtedness owed to the company (or to its affiliates) by the client as its beneficial owner.

A precedent?

70. Mr Trower drew my attention to a scheme of arrangement which Patten J had sanctioned in December 2004. It concerned a company called Wood Gundy (London) Ltd. It appears that Wood Gundy had carried on business as a securities agent, providing a facility for securities to be held in its name, acting as a “marking name” for clients who wished to acquire securities without disclosing their interest in them, and collecting and remitting dividends and other payments in respect of them. The company went into creditors’ voluntary liquidation and the liquidators were faced with the task of returning the securities to clients, not all of whom could be identified and contacted. The purpose of the scheme was to bring about an end to Wood Gundy’s business by distributing all remaining securities (or their proceeds of sale), together with any dividends received, to those who were entitled to them. There was a bar date for claims resulting in the extinguishment of any which were not made by

the stated date. Claimants could elect to claim either the securities which Wood Gundy had been holding for them or, subject to certain exceptions, cash instead. In stated circumstances the client was deemed to have elected the cash alternative. The cash proceeds of securities not claimed by a given date became available for distribution in Wood Gundy's liquidation.

71. I was told that the scheme sanction hearing in that case lasted no more than 20 minutes and was unopposed. No judgment was delivered. Mr Trower did not suggest that the sanctioned scheme – its terms and the fact that it was sanctioned – constituted authority on the scope of the court's jurisdiction under Part 26. He nevertheless referred to the scheme as a matter which I should take into consideration.
72. For what the point is worth, it is to be noted that a client who came forward under that scheme had the right to the return of the very securities to which that client could show an entitlement. The significance of the scheme, if any, for present purposes lies in the extinguishing effect of the bar date on late claims. But as none of the issues debated before me formed the subject of much if any debate, let alone any adversarial debate, before Patten J I can derive no assistance from the fact that the scheme in that case was sanctioned.

Result

73. Insofar as the scheme is concerned with the distribution by LBIE of property held or controlled by it on trust for its clients (and seeks to do so in ways that will vary or, in some cases, extinguish those rights), there is no jurisdiction to enable this to be done, so as to bind dissentients, by recourse to Part 26.
74. Given the exceptional problems that the administrators face in dealing with client assets and the very great effort that they have devoted to devising a means, by way of a scheme under Part 26, to bring about a speedy return of those assets, this is not a conclusion which I am happy to reach. But I must set out the law as I see it, not as I might wish it to be.

A way forward?

75. I do not underestimate the difficulties that the administrators face if they are unable to promote the current scheme. I have endeavoured to summarise them at paragraphs 10 to 16 above. But I question whether they are insuperable.
76. Establishing what the contractual terms are that govern the client's relationship with LBIE, what the net contractual position is between the client and LBIE and what security or similar rights LBIE (and others for whom it is accountable) have over the client's assets in respect of any balance due from the client are tasks to be undertaken in any event under the proposed scheme before there can be any distribution (or appropriation) of the assets in question. Imposing a bar date for claims and establishing a mechanism for valuing claims are matters which, if necessary, can be the subject of a scheme under Part 26.
77. Establishing what client assets of any given client LBIE holds or controls, what competing claims there may be to those assets by other clients or by LBIE (or others) and how LBIE and the administrators are to discharge their duties in respect of those

assets with a view to their due distribution to those entitled to them are all matters where the court has, in the exercise of its trust jurisdiction, well-developed processes to assist the accountable trustee or other fiduciary. For example, the court is well used to authorising a trustee to make distribution of a fund where there can be no certainty that all of the claimants to it have been identified and the trustee desires the protection of a court order in the event that a further claimant should subsequently appear or matters subsequently come to light which question the basis on which the distribution is made. In one sense, dealing with the matter by recourse to the court's assistance in this way can be simpler (and less costly) than the often complex processes involved in the promotion of a scheme under Part 26.

78. At the risk of appearing glib, I do not consider that a structured approach of this broad kind is beyond practical achievement in the exceptionally difficult circumstances of LBIE's administration.