No. 7942 of 2008

IN THE HIGH COURT OF JUSTICE

CHANCERY DIVISION

COMPANIES COURT

IN THE MATTER OF LEHMAN BROTHERS INTERNATIONAL (EUROPE)
(IN ADMINISTRATION)

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

BETWEEN:

(1) ANTHONY VICTOR LOMAS
(2) STEVEN ANTHONY PEARSON
(3) PAUL DAVID COPLEY
(4) RUSSELL DOWNS
(5) JULIAN GUY PARR
(THE JOINT ADMINISTRATORS OF LEHMAN BROTHERS INTERNATIONAL (EUROPE) (IN ADMINISTRATION))

Applicants

-and-

(1) BURLINGTON LOAN MANAGEMENT LIMITED
(2) CVI GVF (LUX) MASTER S.À.R.L
(3) HUTCHINSON INVESTORS, LLC
(4) WENTWORTH SONS SUB-DEBT S.À.R.L
(5) YORK GLOBAL FINANCE BDH, LLC

Respondents

SENIOR CREDITOR GROUP'S POSITION PAPER

This position paper summarises the position of Burlington Loan Management Limited, CVI GVF (Lux) Master S.a.r.l, and Hutchinson Investors, LLC (collectively, the "**Senior Creditor Group**"), in relation to an application for directions made by the joint administrators of Lehman Brothers International (Europe) (the "**Joint Administrators**"

and "**LBIE**", respectively) on 12 June 2014. Unless otherwise stated, this Position Paper adopts the definitions used in Mr Lomas' ninth witness statement. This Position Paper has been updated to reflect the amendments to the formulation of Questions 11 and 12, and the Senior Creditor Group's revised position on Question 20.

STATUTORY INTEREST

Construction of Rule 2.88

Question 1: Whether on the true construction of Rule 2.88(7) of the Rules, Statutory Interest is payable on a simple or compound basis where the rate applicable is specified in section 17 of the Judgments Act 1838? If payable on a compound basis, with what frequency is it to be compounded?

1. **Senior Creditor Group's position:** The rate of interest specified in Section 17 of the Judgments Act 1838 is a simple interest rate.

Question 2: Whether on the true construction of Rule 2.88(7) of the Rules, Statutory Interest is calculated on the basis of allocating dividends:

(i) first to the payment of accrued Statutory Interest at the date of the relevant dividends and then in reduction of the principal;

(ii) first to the reduction of the principal and then to the payment of accrued Statutory Interest; or

(iii) on the basis of some other sequencing.

2. **Senior Creditor Group's position:** For the purpose of calculating the amount of the surplus to be applied in paying statutory interest, dividends paid are treated as having been allocated first to the payment of accrued statutory interest at the dates of payment of the relevant dividends and then in reduction of the principal:

(1) The policy underlying Rule 2.88 is that, where there is a surplus, creditors are entitled to interest to ensure that no person is prejudiced by the effect of the insolvency proceedings, including any delay in the distribution of the estate and payment of proved debts.

(2) Rule 2.88(7) requires the surplus to be applied in paying interest on proved debts in respect of the periods during which they have been outstanding since the relevant date before being applied for any other purpose. It does not describe the method for calculating the amount of the surplus to be applied in paying statutory interest.

(3) The rule for calculating the amount of the surplus to be applied in paying statutory interest where there is a surplus in a distributing insolvency proceeding, whether bankruptcy, administration or liquidation, is that, for that purpose, any payment of dividend is deemed to have been made in satisfaction first of accrued interest and then of principal.

(4) The rule, known as the "*Bower v Marris* Calculation", has, for at least the last 150 years, been applied both in this jurisdiction (including in *Bower v Marris* (1841) Cr & Ph 451; *In re Humber Ironworks and Shipbuilding Co* (1869) LR Ch App 643; and *Re Lines Bros (No.2)* [1948] Ch 438) and in the principal common law jurisdictions (including in *MacKenzie v Rees* (1941) 65 CLR 1; *Re Hibernian Transport Companies Ltd (No.2)* [1991] 1 IR 271; *AG of Canada v Confederation Trust Co* (2003) 65 OR (3d) 519; and *Gerah Imports P/L v The Duke Group Ltd* [2004] 49 ASCR 660).

(5) The rule applies equally whether, in accordance with Rule 2.88(9), the relevant rate of interest is the rate applicable to the debt apart from the administration or the rate specified in Rule 2.88(6).

(6) Absent the *Bower v Marris* Calculation or other forms of compensation (see the Answer to Question 39 below) creditors will be prejudiced by delay in the distribution of the estate and in payment of debts proved and statutory interest.

(7) The rule is in accordance with the policy of the insolvency legislation, and ensures, amongst other things, that, in the event of a surplus:

(a) creditors receive the full amount that they would have been entitled to receive apart from the insolvency proceedings;

(b) creditors are not unjustifiably prejudiced by the effect of the moratorium or from having been unable to issue proceedings, obtain judgment or otherwise enforce their claims;

(c) creditors' entitlement to interest in accordance with Rule 2.88(9) at the rate specified in Rule 2.88(6), which represents statutory compensation for the effect of the moratorium and of the insolvency process, is not unjustifiably prejudiced by the time taken to apply the surplus;

(d) creditors are not treated unequally depending on whether, and if so when, they submitted proofs of debt, had those proofs admitted or received dividends; and

(e) shareholders do not receive part of the surplus at the expense of creditors as a result of the time taken to apply the surplus or otherwise unfairly benefit from the existence or effect of the insolvency proceedings.

(8) The rule was not repealed or altered by the enactment of the Insolvency Act 1986 or Insolvency Rules 1986.

Question 3: Whether the words "the rate applicable to the debt apart from the administration" in Rule 2.88(9) of the Rules refer:

(i) only to a numerical percentage rate of interest; or

(ii) also a mode of calculating the rate at which interest accrues on a debt, including compounding of interest, such that where a creditor has a right (beyond any right contained in Rule 2.88) to be paid compound interest, whether under an Original Contract or otherwise, the creditor is entitled to compound interest under Rule 2.88(7).

3. **Senior Creditor Group's position**: The words "*the rate applicable to the debt apart from the administration*" in Rule 2.88(9) encompass all factors relevant to the rate at which interest accrues, including any numerical percentage component of interest and any mode of calculating interest using such percentage component (which may include compounding):

(1) The phrase "*the rate applicable to the debt apart from the administration*" refers to the rate at which interest accrues on the debt and encompasses all factors relevant to the rate at which interest accrues, including the effect of compounding.

(2) Such an interpretation is required because Rule 2.88(9) requires a comparison between "*the greater*" of the rate applicable under Rule 2.88(6) and that applicable "*apart from administration*" which requires a comparison with a creditor's rights in respect of interest apart from administration.

(3) In the context of a solvent administration, this interpretation of Rule 2.88(9) also respects, so far as possible, a creditor's rights in respect of interest apart from administration, before permitting any sums to be paid to creditors with non-provable or subordinated claims or to be returned to shareholders.

If, contrary to the above, "*the rate applicable to the debt apart from the administration*" does not require one to take into account all of the components which determine the rate at which interest accrues on the debt apart from administration, then the excess (if any) of the amount payable taking all such components into account over the amount actually paid under Rule 2.88(7) ranks as a non-provable claim.

Question 4: Whether the words "the rate applicable to the debt apart from the administration" in Rule 2.88(9) of the Rules are apt to include (and, if so, in what circumstances) a foreign judgment rate of interest or other statutory interest rate.

4. **Senior Creditor Group's position:** The phrase "*the rate applicable to the debt apart from the administration*" in Rule 2.88(9) is capable of including a foreign judgment rate of interest or other statutory interest rate:

(1) Rule 2.88(9) provides that the rate of interest on a debt under Rule 2.88(7) shall be the greater of the rate specified in Section 17 of the Judgments Act 1838 and the rate applicable to the debt apart from the administration.

(2) Rules 2.88(9) and 2.88(7) are intended to ensure that creditors are compensated in line with their rights apart from the administration if and to the extent that the rate apart from the administration is greater than the rate which applies under Section 17.

(3) It is irrelevant whether the source of the rate applicable to the debt apart from the administration is contract, the general law or statute, including a foreign statute.

(4) Whether a foreign judgment rate of interest or other statutory interest rate is a rate applicable to the debt apart from the administration depends on the nature, terms and effect of the relevant provision of the foreign statute as a matter of foreign law.

(5) The provision will provide for a rate which is applicable to the debt apart from the administration if, as a matter of foreign law, the creditor is or would be treated as entitled to interest at that rate apart from the administration.

Question 5: Whether, for the purposes of establishing, as required under Rule 2.88(9) of the Rules, "whichever is the greater of the rate specified under paragraph (6) and the rate applicable to the debt apart from the administration", the comparison required is of:

(i) the total amounts of interest that would be payable under Rule 2.88(7) based on each method of calculation; or

(ii) only the numerical rates themselves,

and in either case, how the total amount of interest is calculated when the "rate applicable to the debt apart from the administration" varies from time to time.

5. **Senior Creditor Group's position:** For the purposes of comparing the rate specified under Section 17 of the Judgments Act 1838 and the rate applicable to the debt apart from the administration and determining which is the greater:

(1) The comparison is with the total amount of interest that would be payable with respect to the debt under Rule 2.88(7) apart from the administration, taking into account all components of the calculation and not merely the numerical percentage component.

(2) To the extent that one or more such components vary from time to time during the relevant period, such variations are to be taken into account in determining the total amount of interest payable apart from the administration and for the purposes of such comparison.

If, contrary to the above, the comparison does not take into account all components of the calculation, the excess (if any) of the amount payable taking all such components into account over the amount actually paid under Rule 2.88(7) ranks as a non-provable claim.

Question 6: Whether, for the purposes of establishing, as required under Rule 2.88(9) of the Rules, "whichever is the greater of the rate specified under paragraph (6) and the rate applicable to the debt apart from the administration", the amount of interest to be calculated based on the latter is calculated from:

(i) the Date of Administration;

(ii) the date on which the debt became due; or

(iii) another date.

6. **Senior Creditor Group's position**: For the purposes of establishing, as required under Rule 2.88(9), "*whichever is the greater of the rate specified under paragraph (6) and the rate applicable to the debt apart from the administration*", the amount of interest based on the latter is calculated by reference to the period or periods for which interest accrued, or would but for the administration have accrued, on or after the Date of Administration. In the context of a solvent administration, and consistent with the Answer to Question 3 above, this interpretation of Rule 2.88(9) respects, so far as possible, a creditor's rights in respect of interest apart from administration.

Period during which the debts "have been outstanding since LBIE entered administration" for the purposes of Rule 2.88(7)

Question 7: Whether Statutory Interest is payable in respect of an admitted provable debt which was a contingent debt as at the Date of Administration from:

(i) the Date of Administration;

(ii) the date on which the contingent debt ceased to be a contingent debt (including in circumstances where the contract was "closed out" after LBIE entered administration; or

(iii) another date,

having regard to whether:

(i) the contingent debt remained contingent at the time of the payment of:

a. the final dividend; or

b. Statutory Interest; and / or

(ii) (to the extent applicable) the Joint Administrators revised their previous estimate of the contingent debt by reference to the occurrence of the contingency or contingencies to which the debt was subject.

7. **Senior Creditor Group's position**: An admitted provable debt that was a contingent debt on the Date of Administration accrues Statutory Interest from the Date of Administration.

(1) Rule 2.88(7) provides that any surplus remaining "*after payment of the debts proved shall, before being applied for any purpose, be applied in paying interest on those debts* [i.e. the debts proved] *in respect of the periods during which they* [i.e. the debts proved] *have been outstanding since the relevant date*". Accordingly, interest is payable on all of the debts proved for the period for which such debts proved have been outstanding since the Date of Administration.

(2) Debts are proved by reference to the amount of the claim as at the date of the Administration (Rule 2.72(3)(b)(ii)) and, where the debt is contingent as at that date, the amount of the claim as at that date is estimated in accordance with Rule 2.81.

(3) "*Debts proved*" are, or are treated as being, unpaid and thus "*outstanding*" since the Date of Administration since this is the date by reference to which, following notice of intention to distribute, they are ascertained and valued and the date when the insolvent debtor's assets are notionally collected and distributed (*In re Humber Ironworks and Shipbuilding Co* (1869) LR 4 Ch App 643; *MS Fashions Ltd v BCCI* [1993] Ch 425; *Stein v Blake* [1996] AC 243).

(4) The application of the hindsight principle means that, where the valuation placed on a contingent debt has been revised from time to time, the revised amount of the debt is or is treated as unpaid and thus outstanding as at the Date of Administration, irrespective of when the contingency vested or when the revision occurred (*MS Fashions Ltd v BCCI* [1993] Ch 425; *Stein v Blake* [1996] AC 243).

Question 8: Whether Statutory Interest is payable in respect of an admitted provable debt which was a future debt as at the Date of Administration from:

(i) the Date of Administration;

(ii) the date on which the future debt ceased to be a future debt; or

(iii) another date,

having regard to whether the future debt remained a future debt at the time of the payment of:

(i) the final dividend; or

(ii) Statutory Interest.

8. **Senior Creditor Group's position:** Statutory Interest is payable in respect of an admitted provable debt which was a future debt as at the date of administration, from the date of administration.

(1) Rule 2.88(7) provides that any surplus remaining "*after payment of the debts proved shall, before being applied for any purpose, be applied in paying interest on those debts* [i.e. the debts proved] *in respect of the periods during which they* [i.e. the debts proved] *have been outstanding since the relevant date*". Accordingly, interest is payable on all of the debts proved for the period for which such debts proved have been outstanding since the date of administration.

(2) Debts are proved by reference to the amount of the claim as at the date of administration (Rule 2.72(3)(b)(ii)) and, where the debt is a future debt as at that date, the amount of the proof or the amount remaining outstanding is, solely for dividend purposes, determined by discounting the debt back to the date of administration in accordance with Rules 2.89 and 2.105.

(3) "*Debts proved*" are, or are treated as being, unpaid and thus "*outstanding*" since the date of administration since this is the date by reference to which, following notice of intention to distribute, they are ascertained and valued and the date when the insolvent debtor's assets are notionally collected and distributed (*In re Humber Ironworks and Shipbuilding Co* (1869) LR 4 Ch App 643; *MS Fashions Ltd v BCCI* [1993] Ch 425; *Stein v Blake* [1996] AC 243).

(4) Statutory Interest is payable in such manner regardless of whether the future debt remains a future debt at the time of the payment of the final dividend or Statutory Interest.

Question 9: Whether a creditor's accession to the CRA (and, in particular, the effect of clauses 20.4.3, 24.1, 25.1, 25.2 and 62.4 of the CRA) would impact upon the answers to questions 7 and 8 above, and if so, how.

9. **Senior Creditor Group's position:** A creditor's accession to the CRA does not affect the Answers to Questions 7 and 8.

MASTER AGREEMENTS

ISDA

Question 10: Whether, on the true construction of the term "Default Rate" as it appears in the ISDA Master Agreement, the "relevant payee" refers to LBIE's contractual counterparty or to a third party to whom LBIE's contractual counterparty has transferred (by assignment or otherwise) its rights under the ISDA Master Agreement.

10. **Senior Creditor Group's position:** On the true construction of the term "Default Rate", the "relevant payee" refers to whichever entity or person is entitled to receive payment of the Early Termination Amount from LBIE:

(1) Both the 1992 and 2002 ISDA Master Agreements ("the ISDA Master Agreements") define the term "Default Rate" to mean "*a rate per annum equal to the cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount*".

(2) The definition of Default Rate refers to the cost "to the relevant payee" and not the "relevant party" (compare the definition of Termination Rate which refers to "*a rate per annum equal to the arithmetic mean of the cost (without*

proof or evidence of any actual cost to each ***party*** *(as certified by each* ***party****) if it were to fund or of funding such amounts*" (emphasis added)).

(3) The word "payee" is not a defined term in the ISDA Master Agreements (compare "Payee" in Section 6(f) of the 2002 ISDA Master Agreement). As a matter of construction, it ought to bear a different meaning to the more commonly used term "party" and the specially defined term "Payee", as those terms are used in the ISDA Master Agreements. As an undefined term, "payee" has its ordinary meaning of "*a person to whom payment is, or is to be, made*" (Stroud's Judicial Dictionary 8th ed.).

(4) The use of the term "payee" (as opposed to the more commonly used term "party" or the specially defined term "Payee") corresponds to the fact that in certain cases, a right to payment can be assigned without a transfer of the entire agreement, with the result, as occurred here, that the assignee would be the "payee" but not a "party." For example, a right to payment from a Defaulting Party can be assigned without a transfer of the entire Agreement, even without the Defaulting Party's consent (Section 7(b) of the ISDA Master Agreements).

Question 11: Is the meaning that should be given to the expression "cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount" capable of including:

(1) *The actual or asserted cost to the relevant payee to fund or of funding the relevant amount by borrowing the relevant amount; and / or*

(2) *The actual or asserted average cost to the relevant payee of raising money to fund or of funding all its assets by whatever means, including any cost of raising shareholder funding; and / or*

(3) *The actual or asserted cost to the relevant payee to fund or of funding and / or carrying on its balance sheet an asset and / or of any profits and / or losses incurred in relation*

to the value of the asset, including any impact on the cost of its borrowings and / or its equity capital in light of the nature and riskiness of that asset; and / or

(4) *The actual or asserted cost to the relevant payee to fund or of funding a claim against LBIE?*

11. **Senior Creditor Group's position:**

(1) The expression "cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount" encompasses any cost that would have been (or is in fact) incurred or sustained by the relevant payee in raising a sum of money equivalent to the relevant amount.

(2) The words "*to fund*" and "*funding*" in the definition of Default Rate encompass the concept of raising a sum of money by any means including debt, equity or other forms of funding.

(3) The concept of "*cost*" in the definition of Default Rate encompasses (and should encompass, in order to ensure that the relevant payee does not bear any part of the costs arising if it were to fund or of funding the relevant amount) any and all costs to the relevant payee of raising a sum of money equivalent to the relevant amount.

(4) With respect to costs that would have been (or are in fact) incurred or sustained by the relevant payee in raising an incremental sum of money equivalent to the relevant amount:

(a) Such costs can be calculated by the relevant payee acting in good faith and rationally and with reference to the basis on which the relevant payee would (or did in fact) raise such a sum;

(b) Such costs are not restricted to any particular form of funding, such as borrowing (there being no good commercial reason to

construe the definition of Default Rate to exclude forms of funding other than borrowing);

(c) Such costs may reflect the relevant payee's overall cost of funding (whether reflecting debt and/or equity), calculated with reference to matters including the risks associated with its business and the return required by its funders in the light of such risks; and

(d) Such costs can and should in any event reflect the true economic cost to the relevant payee of raising such a sum (whether by debt and/or equity), including any change to its overall cost of funding.

(5) It follows that the Senior Creditor Group's position on the reformulated Question 11 is as follows:

(a) As regards 11(1) and 11(2), the expression "cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount" encompasses the actual or asserted cost to the relevant payee of raising money to fund or of funding the relevant amount by whatever means, which may include shareholder funding as well as, or in the alternative to, borrowing or other forms of funding. It may also include any changes to its overall average cost of funding which arise as a consequence of the relevant payee raising money to fund or of funding the relevant amount;

(b) As regards 11(3), the determination of the costs referred to above may take account of the consequences for the relevant payee of carrying a defaulted LBIE receivable on its balance sheet, as where (for example) the relevant payee's cost of borrowing or cost of shareholder funding is increased as a consequence of carrying a defaulted LBIE receivable on its balance sheet; and

(c) As regards 11(4), the Senior Creditor Group contends that the expression "cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount" can include the actual or asserted cost to the relevant payee to fund or of funding a claim against LBIE, in the manner described in paragraph 5(2) above.

Question 12: If and to the extent that the "cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund…the relevant amount" includes a cost of borrowing:

(1) *Should such borrowing be assumed to have recourse solely to the relevant payee's claim against LBIE or to the rest of the relevant payee's unencumbered assets?*

(2) *If the latter, should the cost of funding include the incremental cost to the relevant payee of incurring additional debt against its existing asset base or should it include the weighted average cost on all of its borrowings?*

(3) *Should such cost include any impact on the cost of the relevant payee's equity capital attributable to such borrowing?*

(4) *Is the cost to be calculated based on obtaining:*

(i) overnight funding; or

(ii) term funding to match the duration of the claim to be funded; or

(iii) funding for some other duration?

12. **Senior Creditor Group's position**:

(1) As set out above, the words "*to fund*" and "*funding*" in the definition of Default Rate encompass the concept of raising a sum of money by any means including debt, equity or other forms of funding. They are capable of including (but are not limited to) a cost of borrowing.

(2) As regards Question 12(1), when determining the hypothetical cost of funding the relevant amount, all relevant funding (including borrowing) should be assumed to have recourse to the relevant payee's unencumbered assets generally.

(3) As regards Questions 12(2) and (3):

(a) The Default Rate definition does not compel the relevant payee to certify its cost of funding on the basis of raising a sum equivalent to the relevant amount (actually or hypothetically) by way of borrowing.

(b) Even where a relevant payee elects to do so, the amount it would have to "*pay*" (i.e. coupon and fees) in funding through such borrowing would not constitute its sole "*cost*".

(c) For the reasons explained in the Third Witness Statement of Patrick McKee, additional costs would result from its increased leverage, including:

(i) An increase in the relevant payee's overall cost of borrowing; and

(ii) An increase in the cost of the relevant payee's equity capital.

(d) Such additional costs can also be taken into account when determining a relevant payee's cost of borrowing.

(4) A relevant payee may calculate the cost if it were to fund or of funding the relevant amount on any of the bases set out in Question 12(4), provided such basis is certified by the relevant payee in good faith and rationally (see the Answers to Questions 14 and 15 below). Without limitation, a relevant payee may calculate such cost based on an

assumption of long duration funding, in circumstances where the relevant payee in good faith and rationally expected or would have expected, on the date the relevant amount became due, that the Defaulting Party would take a number of years to repay the relevant amount.

Question 13: Whether the "cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount" should be calculated:

(i) by reference to the relevant payee's circumstances on a particular date; or

(ii) on a fluctuating basis taking into account any changes in the relevant circumstances (and if so, whether the benefit of hindsight applies when taking into account such changes),

in each case, whether or not taking into account relevant market conditions.

13. **Senior Creditor Group's position:** A relevant payee may calculate the cost if it were to fund or of funding the relevant amount on any of the bases set out in Question 13, provided such basis is certified by the relevant payee in good faith and rationally (see the Answers to Questions 14 and 15 below). Without limitation, where a relevant payee calculates such cost based on an assumption of long duration funding, in circumstances where the relevant payee expected or would have expected that the Defaulting Party would take a number of years to repay the relevant amount (see the Answer to Question 12 above), the relevant payee may do so with reference to circumstances and market conditions on the date the relevant amount became due.

Question 14: Whether a relevant payee's certification of its cost of funding for the purposes of applying the "Default Rate" is conclusive and, if not, to what it is subject. In particular whether, in order for a payee's certification to be deemed conclusive, a relevant creditor is under any duty to act:

(i) reasonably;

(ii) in good faith and not capriciously or irrationally; or

(iii) otherwise than in its own interests.

14. **Senior Creditor Group's position:** A relevant payee's certification of its cost of funding is conclusive provided that such certificate is made in good faith and rationally:

(1) The definition of Default Rate precludes any issue of fact with regard to the proper default rate with the phrases "*without proof or evidence of any actual cost*" and "*as certified by it*" (*Finance One Pub. Co. v Lehman Brothers Special Financing Inc.* [2003] WL 21638214).

(2) A relevant payee's certification is conclusive provided that it is made in good faith and rationally, which requires that it is not arbitrary, capricious, perverse or irrational (*Socimer International Bank Ltd v. Standard Bank of London Ltd* [2008] EWCA Civ 116) or subject to manifest error.

Question 15: If the answer to question 14 is that the relevant payee's certification of its cost of funding is not conclusive and one of the requirements (i) to (iii) set out in that question applies, where does the burden of proof lie in establishing, and what is required to demonstrate, that a relevant payee has or has not met such requirement?

15. **Senior Creditor Group's position:** The Defaulting Party bears the burden of proving, on the balance of probabilities, that the relevant payee's certification of the cost if it were to fund or of funding the relevant amount was made otherwise than in good faith or rationally (in the sense set out in the Answer to Question 14 above).

Question 16: Whether only the relevant payee (in accordance with the meaning of such term determined pursuant to question 10 above), or another party (whether authorised by the relevant payee or not) can provide certification of the cost of funding and, if the former, what the position should be if the relevant payee is not capable of providing such certification (for example because it has been wound up or dissolved).

16. **Senior Creditor Group's position:** The relevant payee and anyone expressly or impliedly authorised by the relevant payee can provide certification of the cost of funding.

Question 17: In circumstances where a relevant payee has not incurred any actual costs, what principles should be applied in determining the asserted costs "if it were to fund [...] the relevant amount".

17. **Senior Creditor Group's position:** See the Answers to Questions 11 to 15 above.

Question 18: Whether the power of a party under section 7(b) of the 1992 form ISDA Master Agreement to transfer any amount payable to it from a Defaulting Party under Section 6(e) without the prior written consent of that party included the power to transfer any contractual right to interest under that agreement.

18. **Senior Creditor Group's position:** The power of a party under Section 7(b) of the 1992 ISDA Master Agreement to transfer any amount payable to it from the Defaulting Party under Section 6(e) includes the power to transfer any right to interest on that amount:

    (1) Section 7(b) of the 1992 ISDA Master Agreement provides that "*a party may make such transfer of all or any part of its interest in any amount payable to it from a Defaulting Party under Section 6(e)*".

    (2) Section 6(d)(ii) of the 1992 ISDA Master Agreement provides that "*an amount calculated as being due in respect of any Early Termination Date under Section 6(e) ... will be paid together with ... interest thereon*".

    (3) A party's "*interest*" in an amount payable to it from a Defaulting Party under Section 6(e) therefore includes, in accordance with Section 6(d)(ii), an entitlement to be paid interest on that sum.

(4) There is no commercial rationale for granting a party the power to transfer a right to receive payment of the amount calculated as being due under Section 6(e), whilst at the same time preventing it from transferring its right to interest on that amount.

Question 19: Whether the answer to questions 10 to 18 above (or any of them) is different if the underlying Master Agreement is governed by New York rather than English law.

19. **Senior Creditor Group's position:** The Senior Creditor Group does not contend in these proceedings that the answers it has given to Questions 10 to 18 above are different if the underlying Master Agreement is governed by New York law rather than English law.

German Master Agreement

Question 20: Whether, in calculating the amount of interest due under section 3(4) of the German Master Agreement, it is possible (and if so, in what circumstances and to what extent) to include an amount in respect of "further claims for damages" ("Damages Interest Claim") so that this would constitute part of the "rate applicable to the debt apart from the administration" for the purposes of Rule 2.88(9).

20. **Senior Creditor Group's position:**

(1) The meaning and effect of the German Master Agreement is governed by the law of the Federal Republic of Germany (Section 11(2) of the German Master Agreement).

(2) Under German law, pursuant to sections 280(1) and (2), 286 and 288 of the German Civil Code (**BGB**), creditors with a debt for which default (Verzug) has occurred are entitled to compensation by way of damages for late payment.

(3) The entitlement to damages referred to in paragraph (2) above applies to any defaulted amount, including the close-out amount due pursuant to clauses 7-9 of the German Master Agreement. No provision of the German Master Agreement excludes the entitlement to damages referred to above[1].

(4) Under German law, pursuant to section 280 BGB, a creditor is entitled to damages for late payment of a debt where a "default" has occurred within the meaning of section 286 BGB. As to this:

(a) Whether there has been a "default" (within the meaning of section 286 BGB) by LBIE in respect of any payment obligation under a German Master Agreement before, as at or after[2] the commencement of the administration (including by the issuing of a warning notice (*Mahnung*)) is a question of fact, to be determined on a case-by-case basis.

(b) Under section 271(1) BGB, close-out amounts under clauses 7–9 of the German Master Agreement automatically and immediately fell due upon LBIE applying for an administration order. Under German law, a default occurs in respect of the sum due without the need for issuing any warning notice if either (i) the debtor "seriously and definitively refuses performance" (section 286(2) no 3 BGB) or (ii) if a special reason exists which, when weighing the interests of both parties, justifies the immediate occurrence of a default (section 286(2) no 4 BGB). LBIE's application for an

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[1] For the avoidance of doubt, clause 3(4) does not apply to the close-out amount due pursuant to clauses 7-9 of the German Master Agreement. Even where clause 3(4) does apply, its function is to make clear that the relevant provisions of the BGB referred to above continue to apply subject to a modification of the rate set out in section 288 para 1 BGB.

[2] To date, Wentworth has not identified the provision(s) of German substantive law which it alleges has the effect that any default must occur prior to the commencement of LBIE's administration. The Senior Creditor Group has sought to set out its positive case as to why default will have occurred as a consequence of LBIE applying for and / or entering administration in the following sub-paragraphs but reserves its right to respond further upon receiving clarification from Wentworth of its position.

administration order (made on the basis that it was unable to pay its outstanding debts at the time of making the application) caused either (i) or (ii) (or both) to be satisfied. Accordingly, a default automatically occurred in respect of close-out amounts owed by LBIE upon LBIE applying for an administration order.

(c) Alternatively, the entry into administration by LBIE on 15 September 2008 satisfied the requirements of section 286(2) no 4 BGB (because there was a special reason which, when weighing the interests of both parties, justified the immediate occurrence of a default). Accordingly, and in the alternative to (b) above, a default automatically occurred in respect of close out amounts owed by LBIE upon LBIE entering into administration.

(5) The rate of compensation for late payment of such defaulted close-out amounts is determined in accordance with sections 280(1) and (2), 286 and 288 BGB.

(6) As a matter of German law, the right to compensation granted by section 288(1) BGB is a sub-category of the right to damages for late payment of a defaulted debt under sections 280 and 286 BGB. Section 288(1) BGB provides a statutory minimum rate of compensation for damage caused by the withholding of payment, without the creditor being required to prove the extent of its losses. Accordingly, the BGH has expressly stated that the interest rate under section 288(1) BGB is a "*minimum damage*" and that section 288 (1) and (2) BGB is "*a special form of the principle set out in [old] section 286(1) BGB that the debtor has to compensate any delay damage*"[3].

(7) The compensation provided by section 288(1) BGB is expressed as a rate which is applicable to the debt during the period of default. As a matter of English law, the statutory right to receive such compensation forms part of the creditor's rights as at the commencement of the

[3] BGH, *decision* dated 26 April 1979 – BGHZ 74, 231

administration and, in any event, constitutes part of the "*rate applicable to the debt apart from the administration*" within the meaning of Rule 2.88(9).

(8) Section 288(4) BGB provides that "*the assertion of further damage is not excluded*". In other words, where the rate of damages for late payment of a defaulted debt specified in section 288(1) does not fully compensate a creditor for the loss caused by late payment, such losses may be recovered under sections 280 and 286 BGB.

(9) As a matter of German law, further damages under sections 288(4), 280 and 286 BGB can also, in a number of circumstances, be expressed as a percentage rate of interest accruing on the debt during the period of default. As a matter of English law, the statutory right to receive such compensation forms part of the creditor's rights as at the commencement of the administration and, in any event, constitutes part of the "*rate applicable to the debt apart from the administration*" within the meaning of Rule 2.88(9).

(10) The entitlement to damages referred to above applies to the debt proved (i.e. to the close-out amount) and is part of a creditor's rights as against LBIE at the commencement of the administration. In the circumstances, the nature of the right to damages is such that the Court's existing analysis of Issue 4 of the Waterfall II proceedings is not determinative of whether such a right to compensation constitutes part of the "*rate applicable to the debt apart from the administration*" within the meaning of Rule 2.88(9).

(11) If, contrary to the above, a claim for damages for late payment under Section 288 BGB does not constitute part of the "*rate applicable to the debt apart from the administration*", then such claim ranks as a non-provable claim.

Question 21: If the answer to question 20 is that a further claim for damages can be included as part of the "rate applicable to the debt apart from the administration" for the purposes of Rule 2.88(9), how in such circumstances is the relevant rate to be to be determined? In particular:

(i) in circumstances where the relevant claim under the German Master Agreement has been transferred (by assignment or otherwise) to a third party, is it the Damages Interest Claim which could be asserted by the assignor or the assignee which is relevant for the purposes of Rule 2.88(9)?;

(ii) where the relevant claim under the German Master Agreement has been acquired by a third party, in what circumstances (if any) is such a third party precluded from asserting a Damages Interest Claim under principles of German law?; and

(iii) where does the burden of proof lie in establishing a Damages Interest Claim, and what is required to demonstrate, that a relevant creditor has or has not met such requirement?

21. **Senior Creditor Group's position:**

(1) Where a Damages Interest Claim has been transferred (by assignment or otherwise) to a third party, the third party can assert a Damages Interest Claim calculated by reference to: (a) the Damages Interest Claim of the original counterparty for the period before the date of transfer; and (b) the Damages Interest Claim of the third party for the period (if any) after the date of transfer.

(2) A third party is not precluded from asserting a Damages Interest Claim as a matter of German law where the original parties have consented to the transfer.

(3) The party asserting the Damages Interest Claim has the burden of proof in establishing its loss as a result of any delay in payment. The standard of proof for determining the quantum of loss is, under German procedural law, the balance of probabilities.

<u>French Master Agreements</u>

Question 22: Whether each of:

(i) Default interest pursuant to clause 9.1 of the FBF Master Agreement and the AFB Master Agreement;

(ii) the "Late Interest Rate" as such term is defined in the AFTB Master Agreement; and/or

(iii) "Late Payment Interest" as such term is defined in the AFTI Master Agreement,

are capable of being a "rate applicable to the debt apart from the administration" for the purposes of Rule 2.88(9).

22. **Senior Creditor Group's position:**

(1) The "*rate applicable to the debt apart from the administration*" for the purposes of Rule 2.88(9) includes any entitlement to interest in accordance with the provisions referred to in (i) to (iii) above.

(2) The proper meaning and effect of the FBF, AFB, AFTB and AFTI Master Agreements is a matter of French Law.

(3) As to the FBF and AFB Master Agreements:

(a) clause 9.1 provides that "*in the event of a delay in payment by one of the Parties of any amount due under the Agreement, such party shall pay to the other default interest which shall be due without prior notice, and which shall be calculated on the basis of such sum from and including the date on which the payment should have been made to but excluding the date of effective payment,* ***at the overnight refinancing rate of the Party entitled to receive the relevant amount, in the relevant Currency, plus one per cent. per annum. Interest shall be capitalised if due for a period in excess of a year***" [emphasis added]; and

(b) clause 9.1 of the FBF and AFB Master Agreements is a contractual provision defining the amount of interest on a debt. As such, all amounts calculated pursuant to it constitute part of the "*rate applicable to a debt apart from the administration*" within the meaning of Rule 2.88(9) as a matter of English law.

(4) As to the AFTB Master Agreement:

(a) in the event of a delay in payment of certain sums due under the AFTB Master Agreement, the AFTB Master Agreement requires such sums to be paid along with the "*Late Payment Interest*" (see e.g. clauses 9.1.1 and 12.2.3);

(b) the AFTB Master Agreement defines "Late Payment Interest" as "*interest calculated on any unpaid sum that one party owes to the other at the rate defined in Schedule II A of the Agreement (Late Payment Interest Rate)*";

(c) the "Late Payment Interest Rate" is the "Default Rate" in Schedule II A, which is defined, unless otherwise agreed by the parties, as "*for the euro, the highest rate charged by the European Central Bank for supplying liquidity to the payee of the delayed payment; for other Currencies, the average overnight rate available to the payee of the delayed payment for the period in question*"; and

(d) accordingly, the "Late Payment Interest Rate" is a contractual provision defining the amount of interest on a debt. As such, all amounts calculated pursuant to it constitute part of the "*rate applicable to a debt apart from the administration*" within the meaning of Rule 2.88(9) as a matter of English law.

(5) As to the AFTI Master Agreement:

(a) in the event of a delay in payment of certain sums due under the AFTI Master Agreement, the AFTI Master Agreement requires such sums to be paid along with "*Late-Payment Interests*" [sic] (see e.g. clause 8.2.4);

(b) "Late-Payment Interest" is defined as "*the interest calculated at the rate specified in the appendix on any outstanding amount due from one Party to the other*";

(c) the appendix to the AFTI Master Agreement further defines "Late-Payment Interests" [sic] as "*for French Francs, TMP during the relevant period, plus 1% per annum; for other currencies, the average of the daily rates to which the recipient of the payment has access during the relevant period, plus 1% per annum*"; and

(d) accordingly, "Late Payment interest" under the AFTI Master Agreement is a contractual provision defining the amount of interest on a debt. As such, all amounts calculated pursuant to it constitute part of the "*rate applicable to a debt apart from the administration*" within the meaning of Rule 2.88(9) as a matter of English law.

Question 23: Whether the "party" that receives the interest referred to in question 22 above pursuant to the FBF Master Agreement, the AFB Master Agreement, the AFTB Master Agreement and the AFTI Master Agreement refers to LBIE's original contractual counterparty or to a third party to whom LBIE's original counterparty has transferred (by assignment or otherwise) its rights under the relevant agreements.

23. **Senior Creditor Group's position:**

(1) In the case of the FBF and AFB Master Agreements, the rate of interest payable under clause 9.1 is calculated by reference to the "*overnight refinancing rate of the **Party** entitled to receive the relevant amount…plus one per cent. per annum*" (compounded annually) (emphasis added). Where a transfer of rights under an FBF or AFB Master Agreement from LBIE's original contractual counterparty to a third party has been effected by means of a *cession de contrat* under French law (but not otherwise), the interest payable under clause 9.1.1 is calculated by reference to the

refinancing rate of the original contractual counterparty (compounded annually) for the period before the date of the relevant transfer and by reference to the refinancing rate of the third party (compounded annually) for any period after the date of the relevant transfer.

(2) In the case of the AFTB Master Agreement, the "Late Payment Interest Rate" is "*for the euro, the highest rate charged by the European Central Bank for supplying liquidity* ***to the payee*** *of the delayed payment; for other Currencies, the average overnight rate applicable* ***to the payee*** *of the delayed payment for the period in question*" (emphasis added). The Late Payment Interest Rate under the AFTB Master Agreement is therefore calculated by reference to the rates applicable to the entity entitled to receive payment of the delayed payment.

(3) In the case of the AFTI Master Agreement, Late-Payment Interest is "*for French Francs [now Euros], TMP during the relevant period, plus 1% per annum; for other currencies, the average of the daily rates* ***to which the recipient of the payment has access*** *during the relevant period, plus 1% per annum*" (emphasis added). Late Payment Interest under the AFTI Master Agreement is calculated by reference to the rates applicable to the entity entitled to receive payment of the delayed payment.

Question 24: Whether the terms:

(i) "overnight refinancing rate of the Party" in clause 9.1 as it appears in the FBF Master Agreement and the AFB Master Agreement;

(ii) "the highest rate charged by the European Central Bank for supplying liquidity to the payee" and "average overnight rate applicable to the payee" as they appear in the AFTB Master Agreement;

(iii) "the average of the daily rates to which the recipient of the payment has access during the relevant period" as it appears in the AFTI Master Agreement,

should only be ascertained with reference to the actual or asserted cost of the payee or may be ascertained in other ways.

24. **Senior Creditor Group's position:** The "*overnight refinancing rate of the Party*" as it appears in clause 9.1 of the FBF and AFB Master Agreement, "*the highest rate charged by the European Central Bank for supplying liquidity to the payee*" and "*the average overnight rate applicable to the payee…for the period in question*" as they appear in the AFTB Master Agreement and the "*the average of the daily rates to which the recipient of the payment has access during the relevant period*" as it appears in the AFTI Master Agreement is, in each case, a question of fact to be determined objectively and by reference to the relevant rates which would have been offered to the relevant payees by market participants at the relevant time.

Question 25: Whether only the "party" pursuant to question 23 or another party authorised to act on behalf of the "party" can provide determination and notification of its cost of funding.

25. **Senior Creditor Group's position:** The definitions of "default interest" in clause 9.1 of the FBF and AFB Master Agreements, "Late Interest Rate" in the AFTB Master Agreement and "Late Payment Interest" in the AFTI Master Agreement do not use the language of, or refer to, "*cost of funding*". The *"overnight refinancing rate"* in clause 9.1 of the FBF and AFB Master Agreements, the *"average overnight rate"* in the AFTB Master Agreement and the *"average of daily rates to which the recipient of the payment has access"* in the AFTI Master Agreement is, in each case, a question of fact to be determined objectively and by reference to the relevant rates which would have been offered to the relevant parties by market participants at the relevant time. The "party" pursuant to Question 23 above or another entity expressly or impliedly authorised to act on behalf of the "party" can provide determination and notification of the same.

Question 26: What is the applicable standard, if any, by reference to which any statement by the party as to its "overnight refinancing rate", "average overnight rates" and "average of daily rates to which it has access" is constrained?

26. **Senior Creditor Group's position:**

(1) Where such rates are determined by the Agent pursuant to its duties under clause 5.5 of the FBF and AFB Master Agreements, such determination is binding in the absence of manifest error provided that it is made in good faith and rationally.

(2) Otherwise, the relevant rate is a question of fact to be determined objectively and by reference to the relevant rates which would have been offered to the relevant parties by market participants at the relevant time.

Status of Payee

Question 27: Whether, and if so how, the answers to questions 10 to 26 would be impacted where the "relevant payee" is:

(i) A Credit Institution or Financial Institution;

(ii) A Fund Entity; or

(iii) A corporate or other type of counterparty.

27. **Senior Creditor Group's position:** The Answers to Questions 10 to 26 above apply equally irrespective of whether the "relevant payee" is a Credit Institution, Financial Institution, a Fund Entity, a corporate or any other type of counterparty.

CURRENCY CONVERSION CLAIMS

Question 28: Whether, and if so how, the calculation of a Currency Conversion Claim should take into account the Statutory Interest paid to the relevant creditor by the Joint Administrators.

28. **Senior Creditor Group's position:**

(1) The existence of a Currency Conversion Claim reflects a creditor's right to receive the full amount that it would have been entitled to receive in a foreign currency apart from the administration.

(2) The insolvency regime contains provisions for the payment of Statutory Interest which serve the separate purpose of compensating creditors for being kept out of their money as a result of the insolvency.

(3) Where the amount of interest that a creditor would have been entitled to receive in a foreign currency apart from the administration is less than the amount of Statutory Interest to which it is entitled in the administration, converted into the relevant foreign currency at the date of payment, the creditor has a Currency Conversion Claim solely in respect of principal.

(4) The calculation of such a Currency Conversion Claim in respect of principal is independent of and does not take account of Statutory Interest to which the creditor is entitled (*Re Lines Bros* [1983] Ch 1 and *Re Lines Bros (No.2)* [1984] Ch 438).

(5) Given the different origins and functions of a Currency Conversion Claim and Statutory Interest, the calculation of Currency Conversion Claims in respect of principal should not take into account payments of Statutory Interest.

(6) Where the amount of interest that a creditor would have been entitled to receive in a foreign currency apart from the administration is greater than the amount of Statutory Interest to which it is entitled in the administration, converted into the relevant foreign currency at the date of payment, the creditor has a Currency Conversion Claim in respect of interest (a "Foreign Exchange Interest Claim").

(7) Such a Foreign Exchange Interest Claim will take into account Statutory Interest to which the creditor is entitled.

Question 29: Whether there exists a non-provable claim against LBIE where the total amount of interest received by a creditor applying the Judgments Act Rate on a sterling admitted claim, when

converted into the relevant foreign currency on the date of payment, is less than the amount of interest which would accrue applying the Judgments Act Rate to the original foreign currency claim.

29. **Senior Creditor Group's position:**

(1) A Foreign Exchange Interest Claim will exist where:

(a) the Judgments Act Rate is the rate applicable to a foreign currency claim apart from the administration; and

(b) the amount of interest that the creditor would have been entitled to receive applying the Judgments Act Rate to the foreign currency claim is greater than the amount of Statutory Interest to which it is entitled by applying the Judgments Act Rate to the Sterling admitted claim.

Question 30: Whether there exists a non-provable claim against LBIE where the total amount of interest received by a creditor applying a "rate applicable to the debt apart from the administration" on a sterling admitted claim, when converted into the relevant foreign currency on the date of payment, is less than the amount of interest which would accrue applying the "rate applicable to the debt apart from the administration" to the original foreign currency claim.

30. **Senior Creditor Group's position:** Where the amount of interest that a creditor would have been entitled to receive in a foreign currency apart from the administration is greater than the amount of Statutory Interest to which is it is entitled in the administration, converted into the relevant foreign currency at the date of payment, the creditor has a Foreign Exchange Interest Claim.

Question 31: Whether:

(i) in relation to a GMSLA for which the "Base Currency" is a currency other than sterling, a Currency Conversion Claim can arise in respect of the "Base Currency" if the schedule to

that agreement states that paragraph 10 of that agreement will only apply if LBIE's counterparty is the "Defaulting Party";

(ii) in relation to a GMRA for which the "Base Currency" (as distinct from the "Contractual Currency") is a currency other than sterling, a Currency Conversion Claim can arise in respect of the "Base Currency" if the schedule to that agreement states that paragraph 10 of that agreement will only apply if LBIE's counterparty is the "Defaulting Party"; and

(iii) in relation to other master agreements, a Currency Conversion Claim can arise if the relevant contractual terms state that the termination and close-out netting provisions which would result in a payment obligation in a non-sterling currency by one party to the other do not apply other than upon the default of LBIE's counterparty.

31. **Senior Creditor Group's position:**

(1) It is a question of fact as to which provisions of a GMSLA, GMRA or any other agreement a claim or a proof of debt relates.

(2) Where the Administrators admit a claim pursuant to a provision which, whether expressly or impliedly or whether as a consequence of a course of dealing between the parties or for any other reason, requires payment in a foreign currency and where that claim has been converted into Sterling in accordance with Rule 2.86(1), a Currency Conversion Claim can arise.

Question 32: If the answer to question 31 (i), (ii) and/or (iii) is negative, whether a Currency Conversion Claim can arise (and if so in what circumstances) in respect of such a GMSLA, GMRA or other master agreements.

32. **Senior Creditor Group's position:** See the Answer to Question 31 above.

Question 33: Whether a Currency Conversion Claim can be established by a creditor where the creditor's right is derived from a transfer (whether or not by way of legal assignment) by LBIE's original counterparty (or any assignee of the original counterparty) which only transferred:

(i) the provable debt;

(ii) the right to receive a dividend on the provable debt; or

(iii) the Agreed Claim Amount defined as a numerical amount in a CDD,

and if not, whether the original counterparty or the assignee is capable of having a valid Currency Conversion Claim.

33. **Senior Creditor Group's position:** Pending receipt of Wentworth's Position Paper and in the absence of any particular transfers having been identified, the Senior Creditor Group's position is as follows:

(1) Whether a creditor, whose rights are derived from a transfer, has a Currency Conversion Claim depends on, amongst other things, the true meaning and effect of the transfer, taking into account the factual matrix, determined in accordance with the relevant applicable law or laws.

(2) Without prejudice to paragraph (1) above, a transfer, the terms of which expressly mention only: (a) a provable debt; (b) the right to receive a dividend on a provable debt; or (c) an Agreed Claim defined as a numerical amount in a CDD may, as a matter of construction and depending on the circumstances, impliedly transfer or otherwise entitle the relevant creditor to pursue a Currency Conversion Claim.

EFFECT OF POST-ADMINISTRATION CONTRACTS

Question 34: Whether a creditor's Currency Conversion Claim has been released in circumstances in which the creditor entered into either:

(i) a Foreign Currency CDD incorporating a Release Clause;

(ii) a Sterling CDD incorporating a Release Clause; or

(iii) the CRA.

34. **Senior Creditor Group's position:**

(1) As a matter of construction, taking into account the factual matrix, none of the CDDs released non-provable claims, including Currency Conversion Claims.

(2) The relevant factual matrix included the following:

(a) the purpose of the CDDs, including the Release Clause, was to facilitate the determination of unsecured provable claims for the purposes of paying dividends out of the estate;

(b) the Administrators made it a condition for participating in such dividend distributions that creditors entered into a CDD and told creditors that, if they did not enter into a CDD, their claims would be determined at some unspecified later date with a consequent delay in receipt of any dividend;

(c) CDDs were presented to creditors as non-negotiable documents;

(d) at no stage did the Administrators indicate that CDDs were intended to release or might have the effect of releasing non-provable claims. In fact, in some cases the Administrators expressly acknowledged to creditors that they did not intend to procure the release of non-provable claims;

(e) the purpose of the CDDs, including the Release Clause, did not require the release of non-provable claims;

(f) the CDDs were initially agreed at a time when the Administrators were not projecting a surplus in the LBIE estate (even in a best case scenario) and were telling creditors that they did not envisage that there would be sufficient funds to pay provable debts in full;

(g) if the Release Clause had the effect of releasing non-provable claims, in particular currency conversion claims, this would, in event of a surplus, also have had the effect of treating creditors of LBIE unequally, depending on whether, amongst other things, they entered into a CDD with such a Release Clause;

(h) requiring creditors to release non-provable claims as a condition for participating in dividend distributions would have been inconsistent with the purposes of the administration and with the purposes for which powers had been conferred on the Administrators; and

(i) there would have been no proper reason for the Administrators to require the release of non-provable claims, which would have benefited only subordinated creditors and shareholders at the expense of creditors.

(3) As a matter of construction, taking into account the factual matrix, entry into the CRA gives rise to a Currency Conversion Claim:

(a) the principal purpose of the CRA was to expedite the return of trust assets;

(b) to assist in the process of returning trust assets, the CRA contains provisions modifying a CRA signatory's contractual entitlements so as to determine, in particular, any liabilities of such signatory to LBIE, so that such liabilities could be taken into account when returning trust assets;

(c) the Administrators made it a condition for participating in such an expedited return of trust assets that creditors acceded to the CRA, which was presented to creditors as a non-negotiable document;

(d) the CRA expressly modified contractual entitlements by providing that any claims that were originally denominated in a currency other than USD were modified so that they were denominated in USD (see clauses 4.2, 4.4.2, 24.1 and 25.1). These provisions give a CRA signatory a contractual entitlement to be paid in USD, notwithstanding that any such claim would need to be converted into Sterling for proof of debt purposes;

(e) if the Sterling sum received by the CRA signatory by way of dividends in respect of provable claims is not sufficient to discharge LBIE's contractual liability in USD in full due to foreign exchange rate movements, the creditor has a Currency Conversion Claim;

(f) at no stage did the Administrators indicate that signatories to the CRA would not have a contractual entitlement to be paid the full amount of their claim denominated in USD in accordance with its terms nor that they would be deprived of any non-provable claims; and

(g) the purpose of the CRA did not require signatories to the CRA to be deprived of non-provable claims;

(4) Alternatively, in the event that it is not possible to give effect to the intention of the Administrators and the creditors as a matter of construction:

(a) the common intention of the Administrators and the Senior Creditor Group was that neither a CDD with a Release Clause nor the CRA would release or deprive the Senior Creditor Group of non-provable claims; and

(b) the CDDs and CRA should, in the circumstances, be rectified so as to provide and to have the effect set out above.

Question 35: Whether a creditor's claim to Statutory Interest has been released in whole or in part in circumstances in which the creditor entered into either:

(i) a CDD incorporating a Release Clause; or

(ii) the CRA.

35. **Senior Creditor Group's position:** As a matter of construction, taking into account the factual matrix, none of the CDDs released non-provable claims, including claims in respect of Statutory Interest.

(1) The relevant factual matrix included, in addition to the points made in the Answer to Question 34 above, the following:

(a) from in or around early 2012 the Administrators stated that, in their view, the inclusion of language to preserve a right to Statutory Interest was unnecessary; and

(b) versions of the CDDs used by the Administrators from September 2012 make it clear "*for the avoidance of doubt* … " that claims for Statutory Interest are unaffected by a creditor entering into a CDD.

(2) Further:

(a) CDDs limit the claims of a creditor against the company under the Creditor Agreement to the "Agreed Claim", which is defined as "*the Creditor's Claim … against the Company under and in connection with the Creditor Agreement …*";

(b) claims for Statutory Interest are not claims under or in connection with a Creditor Agreement but are a statutory entitlement, deriving from a Rule in the Insolvency Rules as to the application of a surplus; and

(c) the fact that a creditor has agreed a claim, and an Agreed Claim Amount has been produced, does not prevent Statutory Interest from accruing on that Agreed Claim Amount.

(3) Any other construction would be contrary to the Administrators' intention, namely that "*it was never our intention that creditors would waive their right to Statutory Interest by virtue of the Release Clause*" (Lomas 10 at [69]) and the view, expressed by them from at least early 2012, that "*the inclusion of language to preserve a creditor's right to Statutory Interest was unnecessary on the basis that the release did not waive any entitlement a creditor may have to Statutory Interest*" (Lomas 10 at [67]).

(4) As a matter of construction, taking into account the factual matrix, the CRA did not release a claim to Statutory Interest. In particular clauses 20.4.7 and 25.1 expressly preserve the right to claim Statutory Interest in respect of a Close Out Amount and a Net Financial Claim.

(5) Alternatively, in the event that it is not possible to give effect to the common intention of the Administrators and the creditors as a matter of construction, the CDDs and CRA should be rectified so as to provide as set out above.

Question 36: If a CDD or the CRA has the effect of releasing a Currency Conversion Claim, Statutory Interest claim or other non-provable claims, whether such release(s) should in the circumstances be enforced.

36. **Senior Creditor Group's position:**

(1) If the CDDs have the effect of releasing non-provable claims, the Administrators should (and the Court should direct the Administrators to) refrain from taking advantage of LBIE's strict or technical legal rights by seeking to enforce such releases in circumstances where such

enforcement would confer a windfall benefit on subordinated creditors or shareholders at the expense of the general unsecured creditors:

(a) the Administrators (as they have expressly acknowledged to creditors) never intended to procure the release of non-provable claims, including claims for Statutory Interest and Currency Conversion Claims;

(b) at no stage did the Administrators indicate that CDDs were intended to release or might have the effect of releasing non-provable claims;

(c) the Senior Creditor Group never intended to release non-provable claims or understood that they were being required to release non-provable claims;

(d) if CDDs did have the effect of releasing non-provable claims, the effect of requiring creditors to enter into CDDs on a non-negotiable basis as a condition of participating in dividend distributions would have been to require them to choose either: (a) to receive a dividend but give up any non-provable claim; or (b) run the risk of not receiving any compensation for delay in having their claim adjudicated at some unspecified later date, in the event that there was no surplus (as the Administrators were indicating at the time);

(e) if the Release Clause had the effect of releasing non-provable claims, in particular currency conversion claims, this would, in event of a surplus, have had the effect of treating creditors of LBIE unequally, depending on whether, amongst other things, they had entered into a CDD with such a Release Clause or not;

(f) requiring creditors to release non-provable claims as a condition for participating in dividend distributions was inconsistent with

the purposes of the Administration and with the purposes for which powers had been conferred on the Administrators;

(g) there was no proper reason for the Administrators to require the release of non-provable claims, which would have benefited only subordinated creditors and shareholders at the expense of creditors; and

(h) in the circumstances, the Administrators should (and the Court should direct the Administrators to) refrain from taking advantage of LBIE's strict or technical legal rights under such releases and thereby obtaining a windfall for the benefit of subordinated creditors or the shareholders (*Ex parte James* (1874) LR 9 Ch App 609).

(2) If the CRA has the effect that signatories to the CRA do not have a contractual entitlement to be paid the full amount of their claim denominated in USD or an entitlement to be paid Statutory Interest or otherwise have been deprived of non-provable claims, in the circumstances the Administrators should (and the Court should direct the Administrators to) refrain from taking advantage of LBIE's strict or technical legal rights by seeking to give the CRA such an effect:

(a) the Administrators never intended to modify the CRA signatories' entitlements in such a way as to deprive them of non-provable claims (including claims for Statutory Interest and Currency Conversion Claims);

(b) at no stage did the Administrators indicate that the CRA was intended to or might deprive signatories of non-provable claims;

(c) the Senior Creditor Group never intended the CRA to deprive them of non-provable claims or understood that this was its required effect;

(d) the principal purpose of the CRA was to expedite the return of trust assets and it was a condition of participating in such an expedited return that the signatory acceded to its terms on a non-negotiated basis. Modifying a creditor's contractual entitlements so that there was merely a provable debt in USD but no corresponding non-provable claims (including claims for Statutory Interest and Currency Conversion Claims on such USD amount) as a condition to taking part in an expedited return of trust assets was not necessary to achieve the purpose of the CRA;

(e) depriving signatories to the CRA of non-provable claims would have been inconsistent with the purposes of the administration and with the purposes for which powers had been conferred on the Administrators;

(f) there was no proper reason for the Administrators to deprive signatories to the CRA of non-provable claims, which would have benefited only subordinated creditors and shareholders at the expense of creditors; and

(g) in the circumstances, the Administrators should (and the Court should direct the Administrators to) refrain from taking advantage of LBIE's strict or technical legal rights under the CRA and thereby obtaining a windfall for the benefit of subordinated creditors or the shareholders (*Ex parte James* (1874) LR 9 Ch App 609).

Question 37: How are claims to be calculated where a CDD (or any other agreement pursuant to which an unsecured claim is agreed or admitted) compromises a number of claims, with differing rates of interest applicable or in different currencies, without indicating how the agreed or admitted claim amount in the CDD (or any other agreement) derived from and relates to those underlying claims?

37. **Senior Creditor Group's position:**

(1) Where a creditor has had multiple debts admitted as a single amount under a CDD (or any other agreement pursuant to which an unsecured claim is agreed or admitted) without indicating how the agreed or admitted claim amount derives from or relates to the underlying debts:

(a) the admitted claim is to be divided into its component debts. For the purposes of such division, the value of each component debt is the amount of the admitted claim attributable to that component debt;

(b) the "*rate applicable to the debt apart from the administration*" within the meaning of Rule 2.88(9) is to be determined separately for each component debt, on the basis identified in the Answers to Questions 3 and 4 above; and

(c) the comparison between the "*the greater*" of the rate applicable under Rule 2.88(6) and that applicable "*apart from the administration*" is to be undertaken under Rule 2.88(9) separately for each component debt, on the basis identified in the Answers to Questions 5 and 6 above, and each component debt is entitled to interest under Rule 2.88(7) accordingly.

(2) Where a creditor has had a single claim admitted under a CDD which includes a foreign currency debt, the part of the admitted claim in respect of which a Currency Conversion Claim may arise is calculated by reference to the amount of the admitted claim attributable to the foreign currency debt (or, if more than one, each such amount).

Question 38: Whether (and if so in what circumstances) Part VII of the CRA, which specifies that claims of acceding creditors are to be calculated in US dollars, is capable of giving rise to a Currency Conversion Claim.

38. **Senior Creditor Group's position:**

(1) The effect of the CRA was to modify contractual entitlements by providing that any claims that were originally denominated in a currency other than USD were modified so that they were denominated in USD (see clauses 4.2, 4.4.2, 24.1 and 25.1). These provisions give a CRA signatory a contractual entitlement to be paid in USD, notwithstanding that any such claim would need to be converted into Sterling for proof of debt purposes.

(2) If the Sterling sum received by a CRA signatory is less the amount of its contractual entitlement in USD under the CRA due to foreign exchange rate movements, it will have a Currency Conversion Claim.

COMPENSATION FOR TIME TAKEN TO DISCHARGE NON-PROVABLE CLAIM

Question 39: Whether a creditor entitled to Statutory Interest, Currency Conversion Claims and / or other non-provable claims is entitled to any form of compensation for or in respect of the time taken for such claim to be discharged and, if so, whether such compensation is taken into account as part as the correct methodology for calculating Statutory Interest and / or the distribution of the surplus, or should take the form of interest at the Judgments Act Rate, damages for loss, restitution or another form.

39. **Senior Creditor Group's position:**

(1) The *Bower v Marris* Calculation seeks to protect creditors from being unjustifiably prejudiced as a consequence of any period between the payment of debts proved and the payment of interest on those debts.

(2) The following paragraphs are without prejudice to the Answer to Question 2 above and the *Bower v Marris* Calculation.

Statutory Interest

(3) Creditors have a non-provable claim for damages for loss caused by the non-payment of Statutory Interest in respect of the period between the date of payment of debts proved and the date on which Statutory Interest is paid (*Sempra Metals v Inland Revenue Commissioners* [2008] 1 AC 561).

Claims Denominated In A Foreign Currency

(4) A creditor with a claim denominated in a foreign currency was entitled to payment in the relevant foreign currency on the date that his claim fell due for payment.

(5) Such a creditor has a non-provable claim for loss and damage suffered as a result of the non-payment of his claim on that date (*Sempra Metals v Inland Revenue Commissioners* [2008] 1 AC 561).

General

(6) The existence of such claims is in accordance with the policy of the insolvency legislation as set out in the Answer to Question 2 above.

(7) The amount of loss and damage caused by such non-payment may (without limitation), in each case, be assessed by reference to the Judgments Act Rate.

(8) Alternatively, creditors should be entitled to receive the increase in the value of the assets of the LBIE estate attributable to their non-provable claims. Such assets are held by the Administrators for the benefit of creditors and would otherwise be paid to LBIE's subordinated creditors at the creditors' expense.

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