

No. 7942 of 2008

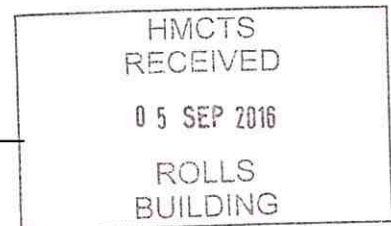
IN THE HIGH COURT OF JUSTICE

CHANCERY DIVISION

COMPANIES COURT

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

AND IN THE MATTER OF THE INSOLVENCY ACT 1986



TENTH WITNESS STATEMENT OF

RUSSELL DOWNS

I, Russell Downs, of PricewaterhouseCoopers LLP ("PwC"), 7 More London Riverside, London SE1 2RT say as follows:

A. INTRODUCTION

- 1 I am a licensed insolvency practitioner and a partner in PwC LLP, a professional services firm at the above address. I am one of the administrators of Lehman Brothers International (Europe) (in administration) ("LBIE").

- 2 My partners, Anthony Victor Lomas, Steven Anthony Pearson and Julian Guy Parr are the other administrators of LBIE. We were appointed as such by orders of the High Court of England and Wales dated 15 September 2008, 2 November 2011 and 22 March 2013. I am duly authorised to make this witness statement on behalf of LBIE and the Administrators.

- 3** I started working on the administration of LBIE in late 2010 and took responsibility for LBIE's relationships with its affiliates, including Lehman Brothers Inc. ("**LBI**") and its trust assets (including client money), on a day to day basis together with Richard Amat, a Lehman Brothers group (the "**Lehman Group**") Managing Director retained among a number of staff by the Administrators. I was appointed as an Administrator in November 2011.
- 4** On 15 September 2008, Lehman Brothers Holdings Inc. ("**LBHI**"), the parent company of both LBIE and LBI, filed for bankruptcy. On 19 September 2008, the United States ("**US**") District Court for the Southern District of New York entered an order granting the application of the Securities Investor Protection Corporation for issuance of a protective decree adjudicating that the customers of LBI are in need of protection afforded by the US Securities Investor Protection Act of 1970 ("**SIPA**") and appointing James W. Giddens of Hughes Hubbard & Reed LLP as trustee (the "**LBI Trustee**"). The liquidation of LBI (the "**SIPA Liquidation**") is presently pending in the US Bankruptcy Court for the Southern District of New York (the "**US Bankruptcy Court**") before The Honorable Shelly C. Chapman (Case No. 08-01420 (SCC) (SIPA)).
- 5** This witness statement is intended to provide factual background to the Court for the purposes of determining the application for directions (the "**Application**") issued by the Administrators pursuant to paragraph 63 of Schedule B1 to the Insolvency Act 1986 to resolve a number of issues which arise in relation to claims Barclays Capital Inc. ("**Barclays**") has against LBIE and/or the Client Money Pool held by LBIE, having acquired such claims from LBI shortly after the collapse of the Lehman Group. Save where otherwise provided, capitalised terms have the meanings ascribed to them in the Application.
- 6** The issues raised in the Application have been the subject of limited correspondence with Barclays as set out in Section D of this statement.
- 7** There is now shown to me a paginated bundle of copy documents, marked "**RD10**" to which I refer in this witness statement. Where no cross-reference to the paginated bundle is provided and where there is no other indication of the source of my information or belief, the contents of this witness statement are derived from facts and matters which are within my own knowledge and belief. These facts and

matters have been learned either as a result of the work undertaken by me as one of the Administrators, or they have been provided to me by my partners and colleagues at PwC or employees of LBIE involved with the administration of LBIE, or by the Administrators' legal advisers, Linklaters LLP ("**Linklaters**").

- 8** Nothing that I say in this witness statement is intended to be a waiver of any privilege to which LBIE and/or the Administrators are entitled and no such privilege is waived.
- 9** I structure the remainder of this witness statement as follows:
- 9.1 Section (B)** outlines the factual background to the Application;
- 9.2 Section (C)** broadly sets out the issues raised in the Application;
- 9.3 Section (D)** outlines the correspondence between LBIE and Barclays in relation to the Application to date;
- 9.4 Section (E)** deals with procedural matters relating to the Application; and
- 9.5 the Appendix** sets out a summary of the issues raised by the Application.

B. BACKGROUND TO THE APPLICATION

Relationship between LBIE and LBI pre-administration

- 10** Prior to LBIE's entry into administration (the "**LBIE Administration**") and the commencement of the SIPA liquidation, LBIE and LBI functioned as part of an integrated, international financial group. LBIE was the principal trading company and broker-dealer within the Lehman Group in Europe. LBI was one of the principal trading companies and a broker-dealer within the Lehman Group in the US.
- 11** As the Lehman Group's regulated broker dealer in Europe, one of LBIE's major business areas was prime services, which involved LBIE acting as prime broker to institutional customers, mostly hedge funds. In order to conduct its various businesses, LBIE needed access to exchanges, clearing systems and depositories in other jurisdictions, directly or through other financial institutions. In particular, when LBIE or its customers sought to gain exposure to securities listed, or

derivatives traded on exchange, in the US or for their US assets to be held for safekeeping, LBI acted as LBIE's primary clearing broker and custodian providing such clearing and custody services to LBIE. Conversely, when LBI or its customers sought to gain exposure to securities listed, or derivatives traded on exchange, in Europe or Asia, or for their European or Asian assets to be held for safekeeping, LBIE acted as LBI's primary clearing broker and custodian providing such clearing and custody services to LBI.

- 12 In accordance with the practices described above, LBIE acted as LBI's European and Asian broker and custodian, providing custody and settlement services to LBI for a number of instruments and financial products, including ETDs.
- 13 The ETD business conducted by LBIE on behalf of LBI included trading futures, options, and forward deliverables (comprising commodities, energy and non-precious metals) (the "**ETD Business**"). Attached at **Annex 1** of this statement is a table setting out the exchanges through which, and currencies in which, positions held in each of the ETD Accounts traded.
- 14 Some of the positions held by LBIE, on behalf of LBI, related to trades entered into by LBI's customers. LBI also traded for its own ("house") account. Accordingly some of the cash and securities held by LBIE for LBI related to LBI's customers whereas other cash and securities related to LBI's own proprietary trading.

Barclays' acquisition of LBI's ETD Business

- 15 On 16 September 2008, LBHI, LBI and Barclays executed an Asset Purchase Agreement (the "**APA**") (Exhibit "RD10" at **pages 1 to 49**) which provided for an emergency sale (the "**Asset Sale**") of certain of LBI's business pursuant to Section 363 of the US Bankruptcy Code, 11 U.S.C. para 363 (the "**Code**"). The APA was amended by a First Amendment to the APA dated 19 September 2008 (Exhibit "RD10" at **pages 50 to 53**), and further clarified and supplemented by a letter agreement dated 20 September 2008 (the "**Clarification Letter**") (Exhibit "RD10" at **pages 54 to 69**).
- 16 The Asset Sale has been described as the "*largest, most expedited and probably the most dramatic asset sale that has ever occurred in bankruptcy history...*" (In *Re Lehman Bros. Holding Inc.*, 445 B.R. 143, 148-49 (Bankr. S.D.N.Y. 2011)). It

was approved by order of the US Bankruptcy Court dated 19 September 2008 (Exhibit "RD10" at **pages 70 to 71**).

- 17** Pursuant to clause 2.1 of the APA (Exhibit "RD10" at **page 15**), Barclays purchased, acquired and accepted from LBI and LBI sold, transferred, assigned, conveyed and delivered to Barclays, all of LBI's right, title and interest in, to and under the "*Purchased Assets*" free and clear of all liens and other interests pursuant to Section 363(f) of the Code. Paragraph 1(a)(ii)(C) of the Clarification Letter provided that "Purchased Assets" included "*exchange-traded derivatives (and any property that may be held to secure obligations under such derivatives)*" (Exhibit "RD10" at **page 55**).
- 18** Litigation in the US ensued between Barclays, LBHI and LBI to determine precisely what assets were transferred to Barclays in the Asset Sale. Among others, a dispute arose over whether the APA transferred to Barclays margin assets of approximately USD 4 billion supporting the ETD Business (the "**LBI Margin Assets**"). The LBI Margin Assets had been maintained by LBI in accounts at various financial institutions as collateral in connection with its ETD Business to support its own and its customers' ETD trading obligations. Some of the LBI Margin Assets were held by LBIE.
- 19** I deal with the outcome of that litigation at paragraphs 33 to 42 below.
- LBIE and LBI's claims against each other
- 20** On 30 January 2009, LBIE filed an omnibus customer claim against LBI in respect of its customers (as amended, the "**Omnibus Claim**"), together with a claim on its own behalf (as amended, the "**House Claim**"), to recover "customer property" as defined in SIPA. The Omnibus Claim was for cash and securities valued at approximately USD 15.1 billion and the House Claim was valued at approximately USD 8.9 billion. In addition, LBIE simultaneously filed a failed trades claim with respect to over 100,000 "*failed to deliver to LBI*" trades and over 95,000 "*failed to receive from LBI*" trades with settlement dates from 19 August 2008 to 24 September 2008.
- 21** In turn, on 31 July 2012, LBI submitted a proof of debt in the Administration in respect of its unsecured claims against LBIE. In addition, LBI asserted trust asset

claims for certain securities held immediately prior to the LBIE Administration and a client money claim comprising, among others, claims in respect of exchange-traded derivatives valued by LBI at approximately GBP 1,042 million (approximately USD 1,870 million) which erroneously included claims in respect of positions held for LBIE clients (totalling USD approximately 794 million).

LBIE and LBI settlement

- 22** Establishing the population of LBI's ETD accounts with LBIE was part of a very significant reconciliation exercise conducted between LBIE and LBI in order to agree, to the extent possible, the various elements of LBI's claims against LBIE and vice versa.
- 23** LBIE conducted a thorough exercise in order to identify all LBIE-maintained accounts as of 12 September 2008 through which LBI had conducted its ETD Business (identified and defined in the LBI/LBIE Settlement (as defined below) as the "*LBI/LBIE ETD Accounts*"). A reconciliation exercise was also undertaken by LBIE and LBI to agree and value the cash balances and the unrealised profit and loss in the "*LBI/LBIE ETD Accounts*" (the "**LBI/LBIE Reconciliation**"). The LBI/LBIE Reconciliation resulted in the parties agreeing for the purposes of settlement (including for the purposes of establishing the reserve discussed at paragraph 27 below) that the value to be attributed to the "*LBI/LBIE ETD Accounts*" was approximately USD 777 million. The parties entered into a settlement agreement on 21 February 2013 (the "**LBI/LBIE Settlement**") (Exhibit "RD10" at **pages 72 to 180**).
- 24** The LBI/LBIE Settlement, after notice and hearing, was approved in an order issued by the then presiding Honorable James M. Peck, US Bankruptcy Court on 16 April 2013 (the "**LBI/LBIE Settlement Order**") (Exhibit "RD10" at **pages 181 to 189**). Further, on 1 May 2013, Mr Justice David Richards (as he then was) made an order providing that the Administrators were at liberty to use their powers so as to cause LBIE to perform its obligations under the LBI/LBIE Settlement (Exhibit "RD10" at **pages 190 to 192**).
- 25** The LBI/LBIE Settlement effected a global resolution of disputes between LBIE and LBI (subject to limited exceptions). The settlement recognised LBIE as a

material creditor in LBI's customer estate. In addition, since LBIE's claims against LBI's estate exceeded LBI's claims against LBIE, the settlement recognised LBIE as a material creditor in LBI's general (unsecured) estate. As regards the general estate, by agreeing LBIE's net creditor claim against LBI, LBI received credit (in the form of a reduction of the amount owed by LBI's estate to LBIE) to reflect the value attributed for settlement purposes to the "*LBI/LBIE ETD Accounts*".

- 26** The LBI/LBIE Settlement also recognised that there was a dispute between LBI and Barclays as to the extent (if any) to which the Asset Sale included the "*LBI/LBIE ETD Accounts*". It refers to the "*Barclays LBIE ETD Claim*", which is defined as: "*(i) the Claim asserted by Barclays against LBIE in respect of the LBI/LBIE ETD Accounts as a contingent unsecured claim in the Barclays LBIE Proof of Debt*" (which I deal with at paragraph 44 below), "*or (ii) any Barclays LBIE Client Money Claim*".
- 27** Pursuant to the LBI/LBIE Settlement, all claims by LBI against LBIE were released save for any and all client money claims (which does not include the "*Barclays LBIE Client Money Claim*") which, whilst undetermined by LBIE at that time, were assigned to LBIE's nominee, Laurifer Limited ("**Laurifer**"), a company with which LBIE has entered into a benefit transfer agreement pursuant to which LBIE will receive amounts equal to Laurifer's recoveries under the assigned claims less certain agreed fees and expenses. However the existence of a dispute between LBI and Barclays over the ownership of the "*LBI/LBIE ETD Accounts*" cast uncertainty over the scope of LBI's release of claims against LBIE. In order to compensate LBIE for the risk that any claims with respect to the "*LBI/LBIE ETD Accounts*" would be later found to belong to Barclays rather than LBI upon resolution of the dispute between LBI and Barclays, LBI agreed to hold a reserve of USD 777 million (the "**Required Reserve Amount**") which was to be made exclusively available for either:
- 27.1** making a payment to LBIE in the event that Barclays was able successfully to assert the "*Barclays LBIE ETD Claim*" against LBIE, in accordance with Article 10.08(a)(A) of the LBI/LBIE Settlement (Exhibit "RD10" at **pages 134 to 135**); or
- 27.2** making a payment to Barclays, on the basis that LBI's obligation to hold the reserve would only be extinguished if (and to the extent that) such payment had the effect of reducing LBIE's liability to Barclays in respect of the "*Barclays LBIE*

ETD Claim", in accordance with Article 10.08(c) of the LBI/LBIE Settlement (Exhibit "RD10" at **pages 136 to 137**).

- 28** Regarding set-off, Article 10.6(d) of the LBI/LBIE Settlement (Exhibit "RD10" at **page 132**) sought to prohibit LBIE and/or the Administrators from seeking to set-off against the "*Barclays LBIE ETD Claim*" or against Barclays in relation to any "*Barclays LBIE ETD Claim*":
- 28.1** any liability of LBI to LBIE which did not transfer to Barclays under the APA; or
- 28.2** any "*Extended Lien Provision*" (as defined in the LBI/LBIE Settlement), unless required to do so by a final order of a court of competent jurisdiction.
- 29** The LBI/LBIE Settlement also provided that Article 10.6(d) did not limit the extent to which the Administrators may take into account:
- 29.1** any liability of Barclays assumed by Barclays under the APA;
- 29.2** any close-out costs allocated by the Administrators or LBIE to the "*LBI/LBIE ETD Accounts*"; or
- 29.3** net positive balances on certain transactions or accounts within the "*LBI/LBIE ETD Accounts*" against negative balances on other such transactions or accounts.
- 30** Notwithstanding that it had settled with LBI, LBIE was accordingly protected, to the extent of USD 777 million, in the event that Barclays was entitled to pursue certain ETD claims against LBIE as a result of the APA.
- 31** On 3 April 2013, Barclays entered its objections in respect of the LBI Trustee's motion to approve the LBI/LBIE Settlement (and certain other relief being sought simultaneously by the LBI Trustee) on the grounds that the LBI Trustee had failed to set aside sufficient reserves fully to compensate Barclays if it were to prevail on its litigation claims arising from the Asset Sale (Exhibit "RD10" at **pages 193 to 202**).
- 32** The parties were able to resolve Barclays' objection as to the LBI/LBIE Settlement by amending the draft LBI/LBIE Settlement Order to include certain language relating to Barclays' claims, including: "*[f]or the avoidance of doubt, nothing in this Order or the [LBI/LBIE Settlement] shall act as collateral estoppel, res judicata or*

*judicial estoppel, or prejudice the merits of any rights, defenses or arguments of [Barclays], with respect to (i) the proof of debt submitted by [Barclays] to the Joint Administrators dated July 26, 2012 in respect of [Barclays'] unsecured claims against LBIE, as the same may be amended or modified by any Barclays LBIE Proof of Debt Variation (as such term is defined in the [LBI/LBIE Settlement]) (as so amended, the "Proof of Debt") including, to the extent all or any portion of the claims in the Proof of Debt are entitled to client money status, client money claims therefor, or (ii) any trust claim that Barclays may in the future file with respect to the assets that are the subject of the proof of debt submitted by [Barclays] to the Joint Administrators dated July 26, 2012, provided that nothing in this paragraph (x) affects or shall affect the terms of the [LBI/LBIE Settlement] or the distributions to be made thereunder (or the finality thereof), or (y) shall prejudice the merits of any rights, defenses or arguments of LBIE with respect to the Proof of Debt, including that [Barclays] did not receive a transfer of all or any of the property or rights asserted in the Proof of Debt" (Exhibit "RD10" at **pages 187 to 188**).*

LBI and Barclays settlement

- 33** As noted above, there was litigation between, amongst others, LBHI, LBI and Barclays in the US as regards exactly what Barclays had acquired pursuant to the APA.
- 34** On 5 August 2014, the U.S. Court of Appeals for the Second Circuit affirmed the U.S. District Court's ruling dated 16 July 2012 that the transfer of the LBI Margin Assets to Barclays (including the cash and securities associated with the "LBI/LBIE ETD Accounts", as defined in the LBI/LBIE Settlement) was contemplated in the APA and confirmed in the Clarification Letter (the "**Second Circuit Ruling**") (Exhibit "RD10" at **pages 203 to 223**). LBI's subsequent application for retrial of that issue was denied on 23 September 2014.
- 35** On 5 June 2015, LBI filed with the US Bankruptcy Court a draft settlement agreement resolving its remaining disputes with Barclays regarding the Asset Sale (the "**LBI/Barclays Settlement**") and a related approval motion (the "**Approval Motion**") (Exhibit "RD10" at **pages 224 to 269**). LBI provided LBIE with final drafts of the LBI/Barclays Settlement and the related motion papers on the morning of 5 June 2015, shortly before filing.

- 36** The Approval Motion set a hearing date of 29 June 2015 and an objection deadline of 22 June 2015. LBIE reviewed and commented on the LBI/Barclays Settlement and draft order approving the LBI/Barclays Settlement. On 25 June 2015, LBI submitted amended versions of the LBI/Barclays Settlement and draft approval order to the US Bankruptcy Court reflecting language discussed among LBI, Barclays and LBIE (Exhibit "RD10" at **pages 270 to 328**).
- 37** On 29 June 2015, the US Bankruptcy Court entered an order approving the LBI/Barclays Settlement (the "**Order**") (Exhibit "RD10" at **pages 329 to 337**) and an accompanying stipulation and order setting out the terms of the LBI/Barclays Settlement in full (Exhibit "RD10" at **pages 338 to 350**).
- 38** The Order states that: *"the [LBI Trustee] and Barclays agreed in the [LBI/Barclays Settlement] that, to implement the District Court's Judgment and the orders entered in the Litigation, the [LBI Trustee] would pay Barclays (i) \$506,554,462 and post-judgment interest thereon at the United States federal post-judgment interest rate, pursuant to the District Court's Judgment, and (ii) USD 777,000,000 out of the [Required Reserve Amount] with respect to the Barclays' LBIE ETD Claim"* (Exhibit "RD10" at **page 330**). In addition, it orders:
- 38.1** *"that upon payment by the [LBI Trustee] of the \$777,000,000, (i) the maximum aggregate undischarged liability of [LBIE] and/or the trustee of the UK statutory trust of client money arising under CASS 7 in relation to LBIE (including the LBIE Client Money Trustee) to [Barclays], with respect to the Barclays LBIE ETD Claims shall automatically, unconditionally and irrevocably be reduced by \$777,000,000 and (ii) Barclays hereby releases LBIE (including the LBIE Client Money Trustee) with respect to the Barclays LBIE ETD Claims in such amount"* (Exhibit "RD10" at **page 334**);
- 38.2** *"that, for the avoidance of doubt nothing in the [LBI/Barclays Settlement] or [the] Order affects, waives or reduces Barclays' claim against LBIE to interest relating to the \$777,000,000 referenced in the preceding paragraph (or LBIE's defenses thereto), and nothing in the [LBI/Barclays Settlement] or in [the] Order affects, waives or reduces Barclays' LBIE ETD Claim against LBIE with respect to assets (and interest with respect thereto) in excess of the \$777,000,000 referenced in the preceding paragraph (or LBIE's defenses thereto)"* (Exhibit "RD10" at **page 334**); and

38.3 *"that except for the reduction in, and release of, the maximum aggregate undischarged liability of LBIE, and the receipt by Barclays of \$777,000,000 with respect to the Barclays LBIE ETD Claims provided for by the third sentence of paragraph 5 of the [LBI/Barclays Settlement], nothing in the [LBI/Barclays Settlement] or in [the] Order shall act as collateral estoppel, res judicata or judicial estoppel as between Barclays and LBIE, or prejudice the merits of any rights, defenses or arguments of Barclays or LBIE against each other" (Exhibit "RD10" at **page 334**).*

39 Similar language was also included in the final version of the LBI/Barclays Settlement: see paragraphs 4, 5 and 6 of the LBI/Barclays Settlement (Exhibit "RD10" at **pages 341 to 342**).

40 The LBI/Barclays Settlement accordingly resulted in LBI paying to Barclays the USD 777m that had been held in reserve pursuant to the LBI/LBIE Settlement (defined in the Application as the "**LBI Payment**"). It did so on terms that accorded with the LBI/LBIE Settlement, namely the pro-tanto reduction of LBIE's liabilities to Barclays.

41 I understand that LBI made the LBI Payment pursuant to the LBI/Barclays Settlement on or around 2 July 2015.

42 Prior to the conclusion of the LBI/Barclays Settlement, there was considerable uncertainty as regards the extent to which LBI's ETD Business with LBIE had been acquired by Barclays. However the LBI/Barclays Settlement confirmed the acquisition by Barclays of LBI's ETD Business (including the LBI Margin Assets). Barclays' acquisition of LBI's ETD Business (including the LBI Margin Assets) potentially entitles Barclays to certain claims against the LBIE client money and/or unsecured estates. It is uncertainty regarding the claims against LBIE to which Barclays is now entitled which gives rise to the need for this Application.

Barclays' Unsecured Claim against LBIE

43 In light of the matters explained above, the Administrators now need to determine the claims available to Barclays as a result of: (i) Barclays having acquired LBI's ETD Business; (ii) LBIE having given LBI credit at the time of the LBI/LBIE Settlement for the then-known value of the "*LBI/LBIE ETD Accounts*" (as defined in

the LBI/LBIE Settlement); and (iii) Barclays having subsequently received the LBI Payment.

- 44** As regards the claims that have been asserted by Barclays to date, on 26 July 2012, Barclays filed the Barclays Proof (Exhibit "RD10" at **pages 351 to 501**) in the Administration.
- 45** The Barclays Proof listed the total value of the Unsecured Claim as: (1) GBP 559,061,975.25 in respect of "*The Exchange – Traded Derivatives Account Claim*", (2) GBP 560,294.36 in respect of a "*Liquidation Costs Claim*"; and (3) GBP 96,487.59 in respect of a "*Service Providers Claim*".
- 46** Barclays indicated that it considered that the Exchange – Traded Derivatives Account Claim of GBP 559,061,975.25 (equating to USD 1,002,789,465) may qualify for client money protection under the terms of the rules of (then) the Financial Services Authority (now the Financial Conduct Authority).
- 47** Appended to the Barclays Proof was an annex entitled "*Exchange-Traded Derivative Accounts claim*" (the "**ETD Annex**") (Exhibit "RD10" at **pages 367 to 372**), in which Barclays clarified that its claim in relation to the ETD Business was for sums relating to:
- 47.1** the balance of any accounts maintained by LBIE through which LBI had conducted its ETD Business and which had transferred to Barclays under the APA (comprising both the cash proceeds in respect of the ETD positions and the LBI Margin Assets);
- 47.2** the proceeds from any LBI Margin Assets which took the form of securities;
- 47.3** the value of any ETDs in the accounts referred to in paragraph 47.1 as of the date of the LBIE Administration; and
- 47.4** the proceeds or realisations from any ETDs that were in the accounts referred to in paragraph 47.1 as of or prior to the date of the LBIE Administration,
- together, the "**Unsecured Claim**".
- 48** Further, in the ETD Annex, Barclays stated that it was aware of a number of accounts at LBIE holding LBI Margin Assets as at 19 September 2008. However

Barclays "reserve[d] the right to finalise the true value of its [Unsecured Claim] following the completion of a comprehensive reconciliation of the information which becomes available to Barclays in due course". Barclays noted that it was basing this understanding on information provided to it by LBIE during the course of 2011 and 2012. I noted above that LBIE and LBI were involved in an extensive reconciliation exercise which ultimately led to the execution of the LBI/LBIE Settlement in February 2013. Mindful of Barclays' potential claim in respect of LBI's ETD Business with LBIE, LBIE had in parallel been sharing relevant information with Barclays and seeking to agree the potential value of Barclays' claims.

- 49 LBIE and Barclays entered into a reconciliation exercise in respect of the Unsecured Claim (which at that time remained subject to the uncertainty occasioned by the litigation in the US) which concluded in January 2013. LBIE and Barclays reached agreement that the value of the "LBI/LBIE ETD Accounts" (as defined in the LBI/LBIE Settlement), when taking into consideration closeout costs, was approximately USD 930 million.

Barclays' Client Money Claim against LBIE

- 50 The Barclays Proof and the ETD Annex indicated that Barclays intended to submit "a client money and/or client/trust asset claim" in relation to "the Accounts" and the LBI Margin Assets and the proceeds thereof, as follows:
- 50.1 in the body of the Barclays Proof, "Barclays intends to submit a client money and/or client/trust asset claim in relation to the Accounts and the LBI Margin Assets and the proceeds thereof... In particular, and without prejudice to the above, Barclays intends to assert a client/trust asset claim in respect of the LBI Margin Assets which took the form of securities (and the proceeds thereof) and the proceeds of any exchange-traded derivative transactions which were closed out after the LBIE administration. The amount of any client/trust asset claim has yet to be determined and is subject to further investigation by Barclays. If LBIE makes a client money entitlement determination or a client/trust asset determination, an unsecured claim is submitted equal to the difference between the client money entitlement determination and/or the client/trust asset entitlement determination and the amount of client money and client/trust assets received from the client

money pool and client/trust assets distributed by Barclays" (Exhibit "RD10" at **page 363**); and

50.2 in the ETD Annex, "*Barclays is submitting this contingent unsecured claim as a protective matter in the event and to the extent it is determined that (a) there is any shortfall in recoveries from [the Client Money Claim] or other proprietary claim or (b) Barclays' claim in relation to the balances in some or all of the Accounts and/or the LBI Margin Assets is properly characterized as an unsecured claim under applicable law*" (Exhibit "RD10" at **pages 367 to 368**).

51 By letter dated 18 April 2013 (see Exhibit "RD10" at **pages 502 to 503**), Barclays, referring to the Barclays Proof, asserted without prejudice to and in addition to the Unsecured Claim, a Client Money Claim "*in relation to all cash balances which were - and/or which should have been - held by LBIE as 'client money' in the Accounts and/or as part of the LBI Margin Assets and/or as proceeds of any [ETD] transactions relating to the Business which were closed out on or after 15 September 2008...*".

The ETD Accounts

52 I have explained above how LBIE and LBI reconciled and agreed between them the population of the ETD Accounts. As noted above, the accounts in question were listed in the LBI/LBIE Settlement. There were 11 such accounts and those same 11 accounts were the basis of the reconciliation and valuation exercise conducted between LBIE and Barclays as explained above.

53 The 11 accounts are listed in **Annex 2**, attached to this statement. Annex 2 also sets out, by ETD Account: (i) the amount claimed in the Barclays Proof; (ii) LBIE's current view of the potential unsecured claim value; and (iii) LBIE's current view of the potential Client Money Entitlement. As explained at paragraph 67.1 below, Barclays has now confirmed that it agrees with these values.

54 The 11 ETD Accounts are designated as follows:

54.1 066-022-07000, 066-022-08001 and 066-022-08002, each maintained in relation to trading on behalf of LBI clients (the "**Segregated Customer Accounts**");

- 54.2** 066-022-08000, a combined account maintained in relation to both trading on behalf of LBI clients and LBI's proprietary ETD trading (the "**Combined Account**");
- 54.3** 066-022-07015, 066-022-07003 and 066-022-08004, each maintained in relation to LBI's proprietary ETD trading (the "**LBI House Accounts**"); and
- 54.4** 071-022-07100, 071-022-07101, 071-022-07102 and 071-022-07107, each maintained by LBIE's Korean branch (the "**Korean Accounts**"). The Korean Accounts were maintained in relation to trading on behalf of LBI clients, LBI's proprietary ETD trading, and trading by LBI on behalf of certain other Lehman affiliates.
- 55** The ETD trades recorded in the Segregated Customer Accounts and those ETD Trades entered into by LBI on behalf of its clients which were recorded in the Combined Account are defined collectively in the Application as the "**Client ETD Trades**". The ETD trades recorded in the LBI House Accounts and those ETD Trades entered into by LBI on its own account which were recorded in the Combined Account are defined collectively in the Application as the "**Non-Client ETD Trades**". The ETD trades recorded in the Korean Accounts are defined in the Application as the "**Korean ETD Trades**".
- 56** I refer to the three accounts listed at paragraph 54.1 as 'segregated' as they were accounts in respect of which client money was segregated pursuant to the rules contained in the Client Assets Sourcebook issued by the (then) Financial Services Authority. The remaining eight ETD Accounts were not included in LBIE's client money segregation processes and accordingly no client money was segregated in respect of them.
- 57** The system in which ETD trading was recorded was known as "**RISC**". RISC was hosted at LBI in the US but LBIE had access to it in order to record and monitor ETD trades. Each of the ETD Accounts is an account maintained in the RISC system. RISC was transferred from LBI to Barclays under the APA.
- 58** Within each of the ETD Accounts, currency balances were recorded according to the currencies in which trades were conducted for the account. The system also recorded any open trades in each account and the values of those open positions. RISC also recorded the overall balance of each ETD Account in USD.

- 59 The profit and loss balances and the values of open trades in the ETD Accounts, as recorded in RISC, were a subset of the many balances which fed into the Lehman Group general ledger where the overall USD account balance (in respect of all forms of business) between LBI and LBIE was recorded.
- 60 As far as LBIE is aware, there was no written contract in place between LBIE and LBI which governed the trading of ETDs. LBIE's trading (on behalf of clients) in ETDs would ordinarily be governed by a Master Institutional Futures Customer Agreement ("**MIFCA**"). During the course of the Administration the Administrators have expended considerable effort in seeking to locate all written contracts between LBIE and its affiliates. They have not located a MIFCA between LBIE and LBI and it was not unusual for ETD dealings between members of the Lehman Group to be undocumented.

C. THE APPLICATION

- 61 The Administrators have issued the Application in order to determine the precise nature of Barclays' entitlements as regards the LBIE unsecured estate and the LBIE client money estate. These issues broadly fall into five categories:
- 61.1 whether Barclays has a Client Money Entitlement in respect of the Non-Client ETD trades, the Korean ETD Trades, and/or the Client ETD Trades. Certain issues arise from the fact that LBIE did not, pre-administration, segregate client money for LBI in respect of its Non-Client ETD Trades (the "**Threshold Issues**"). There is some evidence to suggest that LBI was aware of this lack of segregation, and it might be argued that it was not, in the circumstances, entitled to a Client Money Entitlement in respect of those accounts. A further issue arises from the fact that the Korean ETD Trades were recorded in accounts which were maintained by LBIE's branch in Seoul, South Korea and as a result may not be subject to the CASS client money rules due to their territorial ambit (the "**Korean Issue**"). Subject to the answer to the Korean Issue, the Threshold Issues may also need to be determined in respect of the Korean ETD Trades;
- 61.2 whether Barclays has an Unsecured Claim in respect of the Client ETD Trades, the Non-Client ETD Trades and/or the Korean ETD Trades and, if so, on what

basis the Unsecured Claim should be valued if Barclays also has a Client Money Entitlement in respect of those trades;

- 61.3** whether, in the event that Barclays has both an Unsecured Claim and a Client Money Entitlement in respect of some or all of the ETD Accounts, it is able to elect to pursue a Parallel Unsecured Claim against LBIE to the exclusion of the Client Money Entitlement. It may wish to do so given that statutory interest is payable on provable claims but not on client money claims;
- 61.4** in what manner, and from what date, the LBI Payment falls to be applied towards the reduction of any Client Money Entitlement, any Unsecured Claim, and/or any other claims made by Barclays; and
- 61.5** the extent to which Barclays has potential entitlements to the LBIE Surplus, whether in respect of statutory interest pursuant to Rule 2.88(7) or other non-provable claims.
- 62** The Appendix to this statement provides more detail in relation to each of the Issues in the Application, and explains why the Issues have arisen and their practical and/or economic significance in the LBIE Administration.

D. CORRESPONDENCE BETWEEN LBIE AND BARCLAYS TO DATE

- 63** On 6 July 2016 Linklaters, acting on behalf of LBIE, wrote a letter to Boies, Schiller & Flexner (UK) LLP ("**Boies Schiller**"), who act for Barclays in this matter, enclosing: (i) a schedule providing a breakdown of LBIE's calculation of Barclays' potential claims by ETD Account, both on an unsecured basis and on the basis that Barclays has a Client Money Entitlement (the "**Schedule**"); (ii) a copy of the draft application notice; and (iii) a draft of this witness statement (Exhibit "RD10" at **pages 504 to 552**).
- 64** In the letter, Linklaters asked Boies Schiller to confirm:
- 64.1** whether Barclays was considering its entitlement to pursue the Unsecured Claim to the exclusion of its Client Money Entitlement;
- 64.2** that following the reconciliation work completed in 2013, Barclays agreed that there were no other accounts, trades or other matters which could give rise to a

Client Money Entitlement and/or an unsecured claim against LBIE, other than those shown in the Schedule; and

- 64.3** that Barclays agreed that the figures shown in the Schedule were not in dispute.
- 65** In addition, Linklaters asked Boies Schiller to provide any comments on the draft application notice and witness statement, noting that the Administrators reserved their right to issue the Application in such form as they considered appropriate.
- 66** On 20 July 2016, Linklaters sent a further letter to Boies Schiller, enclosing an updated Schedule (Exhibit "RD10" at **pages 553 to 555**). The letter noted that following the completion of LBIE's due diligence on the accounts, Barclays' Client Money Entitlement in respect of account number 066-022-8000 had increased from USD 772,722,790 to USD 783,224,296 (as shown in Annex 2 below).
- 67** On 11 August 2016, Boies Schiller responded to Linklaters' letters of 6 and 20 July 2016 (Exhibit "RD10" at **pages 556 to 665**). In their letter Boies Schiller:
- 67.1** confirmed that Barclays was prepared to agree to the quantification of its Unsecured Claim and Client Money Entitlement against LBIE as set out in the Schedule to Linklaters' letter of 20 July 2016;
- 67.2** expressed the view that certain issues ought to be removed from the Application, as explained in the Appendix to this statement; and
- 67.3** sought the inclusion of three issues, all of which either:
- 67.3.1** were, in the view of the Administrators, already addressed by one or more of the issues in the Application; or
- 67.3.2** are now included in the Application (see Appendix).
- 68** On 1 September 2016, Linklaters responded to Boies Schiller's letter of 11 August 2016 (Exhibit "RD10" at **pages 666 to 669**). This letter explains why the Administrators are not minded, at least at this juncture, to remove the issues Boies Schiller asked to be removed. Those reasons are also summarised in the Appendix.

E. PROCEDURAL MATTERS

- 69** A copy of the Application and my witness statement will be served on Barclays via its solicitors.
- 70** A copy of the Application and my witness statement will also be provided to the Financial Conduct Authority.
- 71** The Administrators also intend to give notice of this Application to LBIE's other creditors via the PwC LBIE website, the website through which the Administrators regularly updates LBIE's creditors on matters relating to the Administration.
- 72** With a view to making progress with the Application, the Administrators propose that a case management conference be scheduled to obtain procedural directions in relation to the hearing of the Application.
- 73** The Administrators will, if appropriate, file further evidence in advance of the hearing of the Application in order to update the Court on any further developments in relation to the matters dealt with in this witness statement.
- 74** In all the circumstances, the Administrators respectfully invite the Court to give case management directions for the determination of the issues identified in the Application.

Party: Applicant
Witness: R. Downs
Statement No: 10
Exhibit: "RD10"
Date: 5 September 2016

STATEMENT OF TRUTH

I believe that the facts stated in this witness statement are true.

Dated 5 September 2016

Signed:.....

RUSSELL DOWNS

Appendix: Summary of the issues in the Application

I comment below on the Issues set out in the Application in relation to which the Administrators are seeking the Court's guidance. All capitalised terms which are not expressly defined herein should be construed in accordance with the Schedule to the Application, which contains a table of definitions.

(A) CLIENT MONEY ENTITLEMENTS

1 Does Barclays have a Client Money Entitlement in respect of (i) the Client ETD Trades; (ii) the Non-Client ETD Trades; and/or (iii) the Korean ETD Trades?

Issue 1 is designed to resolve the Threshold Issues and the Korean Issue (as defined above).

Issue 1 has not been determined in any of the previous applications brought by the Administrators. In *Re LBIE* [2009] EWHC 3228 (Ch), Mr Justice Briggs was asked to adopt an assumption (for the purposes of those proceedings only) that certain affiliates of LBIE were entitled to client money protection. See the judgment at [48]:

"Of course, questions such as whether a particular affiliate was entitled to client money protection may, on a particular interpretation and application of the rules, have huge financial consequences, both for them, for LBIE's other clients, and for its unsecured creditors. For present purposes, it is sufficient for the court to assume, but without deciding, that the participating affiliates are entitled to such protection, in particular because it became a matter of common agreement during the course of this application that the status of affiliate did not, ipso facto and without more, deprive those entities of the status of client within the meaning of CASS7."

At the end of his judgment (at [428]), Mr Justice Briggs noted that his conclusions were:

"... without prejudice to any contractual provision between LBIE and a relevant affiliate to the contrary, or to the consequences of any aspect of the course of their

mutual dealings which might adversely affect the affiliate's right to insist upon the performance of that obligation."

As noted in the statement (paragraph 56), LBIE did not segregate client money for LBI in respect of its Non-Client ETD Trades, and there is some evidence to suggest that LBI was aware of this practice. Issue 1 raises the question of whether there was any implied contract between LBIE and LBI pursuant to which they validly contracted out of the CASS client money protections. Issue 2, which is summarised below, enables the Court to consider whether LBI's awareness of the non-segregation of money relating to its Non-Client ETD Trades threatens the existence of the Client Money Entitlement which Barclays would otherwise have if Issue 1 is answered in the affirmative as regards those trades. Subject to the answer to the Korean Issue, the Threshold Issues may also need to be determined in respect of the Korean ETD Trades.

Further, as regards the Korean Issue, the rules on territorial ambit of CASS provide that CASS applies to every firm (with certain exceptions), in relation to regulated activities carried on by it from an establishment in the United Kingdom or, in the case of a UK firm (other than an insurer), in relation to passported activities carried on by it from a branch in another European Economic Area state. There is a question as to whether the Korean ETD Trades amounted to "*regulated activities carried on by it from an establishment in the United Kingdom*". Issue 1 enables the Court to consider this question.

2 If the answer to Issue 1 is "yes", is Barclays estopped or otherwise precluded from asserting this Client Money Entitlement (or any part thereof) in respect of such ETD Trades?

Issue 2 has been included to cater for the possibility that (i) LBI would have had a Client Money Entitlement pursuant to the CASS rules but is estopped from asserting it, and (ii) such estoppel is binding on Barclays. For example, it could be argued that an estoppel arose by reason of a convention between LBI and LBIE that client money would not be segregated in respect of certain ETD Trades.

As noted in the statement (paragraph 54.2), the Combined Account contains both trades entered into on LBI's own proprietary account and trades entered into on behalf of clients. The Combined Account was not included in LBIE's client money

segregation procedures. To the extent an estoppel arises, its precise extent, including as regards the Combined Account, will need to be determined.

In their letter of 11 August 2016 (see Exhibit "RD10" at **pages 558 to 559**), Boies Schiller asked the Administrators to remove Issues 1 and 2 from the Application. The Administrators declined to accede to this request, for the reasons explained in Linklaters' letter of 1 September 2016 (see Exhibit "RD10" at **pages 667 to 668**). In summary, the Administrators consider that Issues 1 and 2 may have significant economic consequences, and should be resolved by the Court while the necessary personnel and systems remain available to the Administrators. However, the Administrators will give active consideration to any steps which may contribute to the efficient case management of Issues 1 and 2.

- 3 If Barclays has a Client Money Entitlement and a Parallel Unsecured Claim, and the Parallel Unsecured Claim is reduced by any set-off (whether under Rule 2.85 or otherwise), does the Client Money Entitlement fall to be reduced by the same (or any other) amount?**

This question is related to Issue 9 below, and should be read together with the commentary thereon. In the event that any form of set-off is applicable to any unsecured claim that would otherwise be available to Barclays, the Administrators seek directions as to the impact (if any) of such set-off on any related Client Money Entitlement. The Court will need to consider, *inter alia*, whether the proprietary nature of a Client Money Entitlement means that it should be treated differently from a Parallel Unsecured Claim for the purposes of set-off.

(B) UNSECURED CLAIMS

- 4 To the extent that Barclays (i) does not have a Client Money Entitlement in respect of some or all of the ETD Trades; or (ii) has a Client Money Entitlement but is estopped or otherwise precluded from asserting such Client Money Entitlement in respect of some or all of the ETD Trades, does Barclays have an Unsecured Claim in respect of such ETD Trades?**

If Barclays does not have a Client Money Entitlement in respect of the ETD Trades, it is likely that Barclays nevertheless has a contractual unsecured claim in

respect of such ETD Trades (since the ETD Trades are ultimately founded on a contractual relationship, albeit it appears in this case one which is not governed by a written agreement).

The Administrators are not currently aware of any persuasive argument for the contrary analysis. Nevertheless, Issue 4 has been included for the sake of completeness.

5 To the extent that Barclays has a Client Money Entitlement in respect of some or all of the ETD Trades (and is not estopped or otherwise precluded from asserting such Client Money Entitlement), does Barclays also have a Parallel Unsecured Claim?

In the schedule of definitions to the Application, a Parallel Unsecured Claim is defined as “... *an Unsecured Claim by a client against LBIE which exists concurrently with a Client Money Entitlement arising out of the same underlying contractual obligation, and which is not a Shortfall Unsecured Claim*”.

In circumstances where Barclays has a Client Money Entitlement in respect of the ETD Trades (or any of them), the Administrators require directions as to whether there exists a Parallel Unsecured Claim. The potential existence of a Parallel Unsecured Claim and the extent to which such a claim should be admitted for dividend prior to the final distribution of the Client Money Pool (and it being clear what the ultimate value of the Parallel Unsecured Claim is) are central to many of the issues that follow.

At the present time, the Administrators consider that the answer to Issue 5 is “**yes**”. In reaching this conclusion, the Administrators have relied (among other things) on the decision of Mr Justice David Richards (as he then was) in *Re MF Global UK Ltd* [2013] EWHC 2556 (Ch) (“**MF Global**”). One of the key conclusions reached by the Judge in that case assumes that Client Money Entitlements co-exist alongside Parallel Unsecured Claims. See the judgment at [69]:

“... the amount of a provable debt falls to be reduced by the amount of any distributions from the CMP, whether made before or after the proof of debt is submitted.”

Mr Justice David Richards also emphasised that Client Money Entitlements are founded on contractual rights, which is consistent with the foregoing analysis. See the judgment at [55], where the Judge said that it is:

"... the contract which gives rise to the client's right to participate in a distribution of the CMP, as well as to participate in the distribution of the general estate, and it is still by reference to the contract that the client's right of participation is calculated ..."

This Issue has nevertheless been included in the Application in case any stakeholder of LBIE wishes to contend that Barclays has no Parallel Unsecured Claim and is joined to the Application to make that argument. LBIE's position as to whether such joinder would be appropriate is, at this stage, fully reserved.

6 To the extent that the answer to Issue 5 is "yes", on what basis is the Parallel Unsecured Claim to be valued?

In circumstances where an ETD Trade does give rise to both a Client Money Entitlement and a Parallel Unsecured Claim, the Administrators require directions as to how the value of the Parallel Unsecured Claim should be ascertained. In particular, the Administrators require certainty as regards whether the Parallel Unsecured Claim should be valued solely in accordance with the underlying contract, or whether the concurrent Client Money Entitlement should also be taken into account when considering the amount to be admitted to proof.

I understand that the decision of Mr Justice David Richards in MF Global may be relevant in this regard, although I understand that in that case the Judge was dealing with a situation in which both the client money and unsecured claims were being pursued. Depending upon the answer to this question, there may be a degree of overlap with Issues 7(2) and 8(1).

7 If Barclays has both a Client Money Entitlement and a Parallel Unsecured Claim, is Barclays entitled and/or should the Administrators be directed to treat Barclays as being entitled to elect to pursue the Parallel Unsecured Claim to the exclusion of the Client Money Entitlement? If the answer is "yes":

- (1) (a) Is Barclays required to disclaim, surrender, abandon, assign or take any other step in relation to the Client Money Claim before the Parallel Unsecured Claim can be admitted by the Administrators; (b) If so, is Barclays entitled to disclaim, surrender, abandon, assign or take such other step in relation to the Client Money Claim?
- (2) If the value of the Parallel Unsecured Claim is impacted by the Client Money Entitlement, prior to the Client Money Pool being distributed are the Administrators entitled and/or obliged (a) to admit the Parallel Unsecured Claim; and/or (b) to pay a dividend in respect of the Parallel Unsecured Claim? If so, in each case, to what extent should the Client Money Entitlement be taken into account when admitting or paying a dividend in respect of the Parallel Unsecured Claim?
- (3) If the Parallel Unsecured Claim should not be admitted until a particular time or event, what interim steps (if any) are the Administrators entitled and/or obliged to take to make a provision for the Parallel Unsecured Claim?
- (4) If the Parallel Unsecured Claim may be admitted but no dividend(s) may be paid in relation thereto until a particular time or event, what interim steps (if any) are the Administrators entitled and/or obliged to take to make a provision for the Parallel Unsecured Claim?
- (5) If the Administrators pay dividends in respect of the Parallel Unsecured Claim, does the corresponding Client Money Entitlement fall to be reduced by the amount of such dividends (or by any other amount)?

Issue 7 seeks to determine, as a matter of law, whether Barclays can elect to pursue any Parallel Unsecured Claim to the exclusion of its Client Money Entitlement – and, if so, the consequences of such election. It is intended to establish whether Barclays has the right to elect between a Parallel Unsecured

Claim and a Client Money Claim. If it does not have such a right, Boies Schiller has requested that the Court determine whether the Administrators should nonetheless be directed to treat Barclays as having such a right to elect (by reason of the rule in *Re Condon; ex p. James* (1873-74) LR 9 Ch App 609 or paragraph 74 of Schedule B1) (see Boies Schiller's letter of 11 August 2016 (Exhibit "RD10" at **pages 559 to 560**)). This Issue also seeks to establish whether there is any reason, as a matter of fact, why Barclays would not be entitled to make such an election.

In many cases, creditors would prefer to pursue their Client Money Entitlement over any Parallel Unsecured Claim (because proprietary claims are often more valuable than unsecured claims).

In the present case, however, provable unsecured claims have been or will be paid in full and Statutory Interest (at a minimum rate of 8% per annum) will be payable on all debts admitted to proof from the LBIE Surplus. No Statutory Interest will be paid on Client Money Entitlements.

For this reason, many of LBIE's creditors have (on the assumption that they are entitled to do so) chosen to waive their Client Money Entitlements or to assign their Client Money Entitlements to a nominee of LBIE. The Administrators have treated such waivers and assignments as being effective.

If Barclays is entitled and/or the Administrators are directed to treat Barclays as being entitled to elect to pursue any Parallel Unsecured Claim to the exclusion of its Client Money Entitlement, various ancillary questions arise concerning the rights and obligations of Barclays and the Administrators.

- 7.1** First, it is necessary to identify the mechanism by which Barclays can effect its election. Various possibilities are identified in Issue 7(1) – including disclaimer, surrender, abandonment and assignment. Issue 7(1) seeks to determine whether Barclays is required to take any such step, and whether Barclays is entitled to take any such step before its Parallel Unsecured Claim can be admitted to proof.
- 7.2** Second, it is necessary to determine whether the Administrators are entitled or required to admit the Parallel Unsecured Claim prior to the distribution of the Client Money Pool or it otherwise being certain what Barclays will be paid out of the

Client Money Pool. If they are so entitled or obliged, the Administrators also require directions as to what extent the Client Money Entitlement should be taken into account when admitting the Parallel Unsecured Claim. Plainly, no client should make a double recovery.

7.3 In the event that any Parallel Unsecured Claim should not be admitted until a particular time or event (for example, until the Client Money Pool has been fully distributed), the Administrators require directions as to whether they are entitled or required to take any steps in the intervening period in order to provide for the Parallel Unsecured Claim. For example, subject to the answers to the other Issues in the Application, it may be that a reserve is to be established in respect of the Parallel Unsecured Claim based on the Administrators' prudent estimate of the value of the Parallel Unsecured Claim once the Client Money Pool has been fully distributed.

7.4 In the event that any Parallel Unsecured Claim may be admitted but no dividend(s) may be paid until a particular time or event (for example, until the Client Money Pool has been fully distributed), the Administrators similarly require directions as to whether they are entitled or required to take any steps in the intervening period in order to provide for the Parallel Unsecured Claim.

7.5 In this regard, the Administrators require directions as to whether the payment of dividends in respect of the Parallel Unsecured Claim would result in a *pro tanto* reduction of the Client Money Entitlement. (I understand that in MF Global, Mr Justice David Richards held that a distribution from the Client Money Pool results in a *pro tanto* reduction in the quantum of any Parallel Unsecured Claim. However, the Court has not yet determined whether the payment of dividends from LBIE's general estate would have a comparable effect on the value of the relevant Client Money Entitlement.)

8 If Barclays is not entitled to elect to pursue the Parallel Unsecured Claim to the exclusion of the Client Money Entitlement:

(1) Are the Administrators entitled and/or obliged to admit any Unsecured Claim prior to the Client Money Pool being distributed? If so, to what extent should the Client Money Entitlement be taken into account when admitting the Unsecured Claim?

(2) If any Unsecured Claim should not be admitted until a particular time or event, what interim steps (if any) are the Administrators entitled and/or obliged to take to provide for the Unsecured Claim?

8.1 Issue 8(1) mirrors Issue 7(2) in circumstances where Barclays is not entitled to pursue the Parallel Unsecured Claim to the exclusion of the Client Money Entitlement. In those circumstances, the Administrators require directions as to whether they are entitled or required to admit any Unsecured Claim prior to the distribution of the Client Money Pool.

8.2 Issue 8(2) mirrors Issue 7(3). In the event that any Unsecured Claim should not be admitted until a particular time or event (for example, until there has been a final distribution of the Client Money Pool), the Administrators require directions as to whether they are entitled or required to take any steps in the intervening period in order to provide for the Unsecured Claim.

8.3 In their letter of 11 August 2016 (see Exhibit "RD10" at **pages 559 to 560**), Boies Schiller asked the Administrators to remove Issue 7(1) and the whole of Issue 8 from the Application. The Administrators declined to accede to this request, for the reasons explained in Linklaters' letter of 1 September 2016 (see Exhibit "RD10" at **page 668**). In summary, the Administrators consider that Issues 7(1) and 8 form a necessary stage in the analysis of whether Barclays is entitled to receive Statutory Interest on any Unsecured Claim. The Administrators will keep under review how, as a matter of case management, Issues 7(1) and 8 may be progressed most efficiently.

9 If Barclays has an Unsecured Claim (whether a Parallel Unsecured Claim, a Shortfall Unsecured Claim or any other Unsecured Claim):

(1) Is such Unsecured Claim subject to a mandatory set-off under Rule 2.85 against any sums owing by LBI to LBIE?

(2) Is such Unsecured Claim subject to a mandatory set-off under Rule 2.85 against any sums owing by Barclays to LBIE?

(3) Does LBIE have an equitable right to set off such Unsecured Claim against any sums owing by Barclays and/or LBI to LBIE?

(4) Does LBIE have a common law right to set off such Unsecured Claim against any sums owing by Barclays and/or LBI to LBIE?

As explained in the main body of this witness statement, LBI was, as at the Administration date, a net debtor of LBIE. The Administrators require directions as to whether any set-off arises so as to reduce the Unsecured Claims that would otherwise be available to Barclays.

The Administrators are not currently aware of any persuasive argument that any of these types of set-off should apply.

In their letter of 11 August 2016 (see Exhibit "RD10" at **page 559**), Boies Schiller argued that this Issue, together with the related Issue 3 above, ought to be removed from the Application on the basis that there is no legal or factual basis on which set-off could apply to the Unsecured Claims. On balance, however, the Administrators have decided that Issues 3 and 9 should be included so as to bring to light whether any other person takes a different view: see Linklaters' letter of 1 September 2016 (Exhibit "RD10" at **page 668**). If no opposing view emerges, Issues 3 and 9 can be case-managed appropriately. The Administrators are keen to avoid a situation in which a third party seeks to raise Issue 3 or 9 at a later date, thereby postponing the completion of the Administration. The inclusion of Issues 3 and 9 in the Application is intended to reduce that risk.

(C) THE LBI PAYMENT

10 In what manner, and from what date, does the LBI Payment fall to be applied towards the discharge or reduction of:

- (1) Barclays' Client Money Entitlement (if any);**
- (2) Barclays' Unsecured Claim(s) in respect of the ETD Trades (if any);
and/or**
- (3) Barclays' other claims (if any)?**

I explain in my statement the circumstances surrounding the LBI Payment to Barclays. The Administrators require directions as to which claims have been reduced or discharged as a result of that payment. The answer to Issue 10 will

also determine the order in which the relevant claims have been reduced or discharged, and the date from which such discharge or reduction took effect. This Issue is likely to require consideration of the provisions pursuant to which the LBI Payment to Barclays was made and expert evidence of New York law. To be clear, the Administrators understand that Barclays does not take the position that it should be entitled to any double-recovery with respect to the amount received by way of the LBI Payment: see Boies Schiller's letter of 11 August 2016 (Exhibit "RD10" at **page 556**).

- 11 Rule 2.72(3)(b)(ii) provides that a proof of debt must state "*the total amount of [the creditor's] claim as at the date on which the company entered administration, less any payments that have been made to [the creditor] after that date in respect of [the creditor's] claim...*". On the true construction of the latter provision, does the LBI Payment, or any part thereof, constitute a payment in respect of Barclays' claim within the scope of Rule 2.72(3)(b)(ii)?**

Rule 2.72 describes the mechanism for proving a debt in an administration. Rule 2.72(3) sets out the matters which must be stated in a proof of debt, and explains the method for calculating the provable amount.

The Barclays Proof, in its current form, does not deduct any part of the LBI Payment from Barclays' claim (Exhibit "RD10" at **pages 351 to 501**). Accordingly, Issue 11 will determine whether the Barclays Proof complies with Rule 2.72(3)(b)(ii).

- 12 Are the Administrators entitled and/or obliged to admit the Barclays Proof for a reduced amount deducting an amount in respect of the LBI Payment (or any part thereof)?**

The answer to Issue 11 is likely to inform the answer to Issue 12.

For example, if the Court finds that the LBI Payment constitutes a payment "*in respect of*" Barclays' claim within Rule 2.72(3)(b)(ii), then an amount in respect of the LBI Payment should *prima facie* be deducted from the Barclays Proof.

Issue 12 may be relevant to the calculation of Statutory Interest, because Rule 2.88(7) appears to provide that Statutory Interest is only payable on the amount admitted to proof: see Issues 17 to 19 below.

- 13 Does (i) creation of the Dedicated Reserve; and/or (ii) the LBI Payment; and/or (iii) the Administrators' consent thereto; and/or (iv) any other action relating to the creation of the Dedicated Reserve and payment therefrom, itself constitute (a) an admission to proof; and/or (b) payment of a dividend by the Administrators of part of the Barclays Proof in an amount equal to such payment?**

This Issue has been included at the request of Barclays: see Boies Schiller's letter of 11 August 2016 (Exhibit "RD10" at **page 560**).

For the avoidance of doubt, the Administrators do not consider that they have admitted or paid dividends on the Barclays Proof (or any part thereof). Nevertheless, the Administrators are content for Issue 13 to be included in the Application so that it may be determined by the Court.

- 14 If the Barclays Proof should be admitted without deducting an amount in respect of the LBI Payment (or any part thereof), are the Administrators entitled and/or obliged to give credit for the Sterling Equivalent of the LBI Payment (or any part thereof) when paying dividends in respect of the Barclays Proof?**

Barclays is *prima facie* entitled to receive dividends up to the full amount of the sum admitted to proof.

However, if no part of the LBI Payment falls to be deducted from the Barclays Proof, and no credit for the LBI Payment is given when paying the dividend, the payment of dividends in this manner would result in an unfair windfall for Barclays. Barclays would effectively be paid twice: once by LBIE, and once by LBI.

As noted above in Issue 10, the Administrators understand that Barclays does not take the position that it should be entitled to any such double-recovery or "windfall". Barclays contends that the Barclays Proof should be admitted in full,

and that credit for the LBI Payment should be given when any dividends are paid: see Boies Schiller's letter of 11 August 2016 (Exhibit "RD10" at **page 556**).

15 In relation to Issues 10 to 14 and Issue 19, how is the amount in respect of the LBI Payment to be calculated? In particular, if it is the Sterling Equivalent that is to be taken into account, should the Sterling Equivalent of the LBI Payment be calculated based on the exchange rate prevailing at:

- (1) The Time of Administration;**
- (2) The time when Barclays received the LBI Payment; or**
- (3) Some other time?**

I understand that the LBI Payment was made in US Dollars. In the event that the Sterling Equivalent of the LBI Payment falls to be taken into account in any way, the Administrators require directions as to the correct date on which the LBI Payment is to be converted into Pounds Sterling for such purposes.

Given the sums at stake, different exchange rates could make a material difference to Barclays (and therefore to LBIE's unsecured estate). For example, the Administrators calculate the difference between converting the LBI Payment to Pounds Sterling at the date it was paid to Barclays and converting it at the rate applicable at the Time of Administration to be in excess of GBP 60 million.

(D) LBIE SURPLUS ENTITLEMENTS

16 If Barclays has an Unsecured Claim in respect of the ETD Trades, in what currency (or currencies) is such Unsecured Claim denominated (prior to any conversion under Rule 2.86)?

I have explained in the main body of my statement that the ETD Accounts recorded trades in a variety of currencies, but that the overall balance on each ETD Account was recorded in US Dollars. For the purposes of any currency conversion claim that may be available to Barclays, the Administrators seek directions as to the currency or currencies in which any Unsecured Claims are denominated.

17 On the true construction of Rule 2.88(7), if the Barclays Proof should be admitted for a reduced amount by deducting an amount in respect of the LBI

Payment (or any part thereof), is the debt on which Statutory Interest is payable: (i) the amount admitted to proof; or (ii) the amount that would have been admitted to proof but for such deduction?

This question follows from Issue 12 above, which asks whether the Administrators are entitled and/or obliged to admit the Barclays Proof for a reduced amount deducting an amount in respect of the LBI Payment. If the answer to that question is "yes", there arises a further issue as to whether, on the true construction of Rule 2.88(7), Statutory Interest is to be paid on the reduced admitted amount or the amount that would have been admitted but for such deduction.

18 If the Administrators admit the Barclays Proof for a reduced amount by deducting an amount in respect of the LBI Payment (or any part thereof):

(1) Should the Administrators be directed under the rule in *Re Condon*; *ex p. James (1873-74) LR 9 Ch App 609*; and/or

(2) Should the Administrators be directed under paragraph 74 of Schedule B1; and/or

(3) Are the Administrators estopped from refusing

to pay Statutory Interest on some amount other than the sum admitted to proof? If so, how should such amount be calculated, and from what date should Statutory Interest be paid thereon?

This Issue was included at the request of Barclays: see Boies Schiller's letter of 11 August 2016 (Exhibit "RD10" at **page 560**). See the further commentary under Issue 19 below.

19 If the Barclays Proof should be admitted without deducting an amount in respect of the LBI Payment (or any part thereof), on the true construction of Rule 2.88(7), in calculating the principal sum on which Statutory Interest is payable in respect of the Barclays Proof, should such principal sum be reduced by the Sterling Equivalent of the LBI Payment from the date when Barclays received the LBI Payment (or any other date)?

Issues 17 to 19 are among the most important Issues in the Application. The basic underlying question is whether Barclays is entitled to receive Statutory Interest under Rule 2.88(7) on the LBI Payment.

This underlying question can be viewed from different perspectives, depending on the answer to Issue 12:

- (1) If the answer to Issue 12 is “**yes**” (such that the LBI Payment should be deducted from the Barclays Proof), then the critical question is whether Statutory Interest is payable only on the amount which is admitted to proof: see Issue 17.
- (2) If the answer to Issue 12 is “**yes**” (such that the LBI Payment should be deducted from the Barclays Proof) and Statutory Interest is payable only on the amount admitted to proof, then Issue 18 asks whether the Administrators ought to pay Statutory Interest on some other sum (by reason of the rule in *Ex p. James*, paragraph 74 of Schedule B1 and/or the doctrine of estoppel). As noted above, Issue 18 has been included in the Application at the request of Barclays.
- (3) If the answer to Issue 12 is “**no**” (such that the LBI Payment should not be deducted from the Barclays Proof), then the critical question is whether the LBI Payment should be deducted from the principal sum on which Statutory Interest is payable: see Issue 19.

The answers to Issues 17 to 19 ultimately depend on the true construction of Rule 2.88(7), which provides as follows:

“Any surplus remaining after payment of the debts proved shall, before being applied for any purpose, be applied in paying interest on those debts in respect of the periods during which they have been outstanding since the relevant date.”
(emphasis added)

The financial value of Issues 17 to 19 is high. This is a consequence of (i) the substantial predicted surplus in LBIE’s estate; (ii) the high rate of Statutory Interest (no less than 8%: see Rule 2.88(9)); and (iii) the duration of LBIE’s administration and the fact that Barclays’ unsecured claim has not yet been admitted – and therefore has not yet been paid – because of the complex issues raised by this Application.

If Barclays is entitled to have the Barclays Proof admitted in full (without any reduction in respect of the LBI Payment) and the Court determines that Statutory

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Interest is payable on the full amount of the Barclays Proof, Statutory Interest of an amount in excess of GBP 300 million could become payable to Barclays from the LBIE Surplus.

**Annex 1: Summary of the exchanges through/currencies in which positions
 recorded in the ETD Accounts were traded**

1 Open positions as at the Time of Administration

Account	Exchange	Currency
066-022-07000	German Derivatives Exchange ("DTB")	EUR
	European Energy Exchange	EUR
	Swiss Options and Financial Futures Exchange ("SOFX")	CHF
066-022-07003	DTB	EUR
	SOFX	CHF
066-022-08000	European Options Exchange ("EOE")	EUR
	Intercontinental Exchange	EUR, GBP, USD
	London Commodities Futures & Options Exchange	GBP, USD
	London International Financial Futures and Options Exchange	CHF, EUR, GBP, USD
	London Metal Exchange ("LME")	USD
	London Traded Options Market	GBP
	Marché à Terme International de France ("MATF")	EUR
	Mercado Espanol de Futuros Financieros ("MEFF")	EUR
	Milan Stock Exchange("MILN")	EUR
	French MONEP CAC ("MONP")	EUR
	Aktiebolaget Optionsmäklarna/Helsinki Stock Exchange ("OM")	NOK, SEK
PowerNext Futures Exchange	EUR	

Account	Exchange	Currency
	Taiwan Futures Exchange ("TWFE")	TWD
066-022-08001	LME	USD
066-022-08002	EOE	EUR
	MATF	EUR
	MONP	EUR
	OM	NOK, SEK
066-022-08004	Athens Derivatives Exchange	EUR
	Australian Derivatives Exchange	AUD
	BM&F BOVESPA	BRL
	MEFF	EUR
	MILN	EUR
	South African Futures Exchange	ZAR
	Turkish Derivatives and Options Exchange	TRY
	TWFE	TWD
	Warsaw Stock Exchange	PLN
071-022-07101	Korean Stock Exchange ("KSE")	KRW
071-022-07107	KSE	KRW

2 Currencies of cash balances as at the Time of Administration

Account	Currency
066-022-07000	CHF
	EUR
	GBP
	USD
066-022-07003	CHF

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Account	Currency
	EUR
066-022-07015	EUR
066-022-08000	AUD
	BRL
	CHF
	DKK
	EUR
	GBP
	JPY
	NOK
	SEK
	TWD
	USD
	ZAR
066-022-08001	CHF
	DKK
	EUR
	GBP
	JPY
	NOK
	SEK
	USD
	ZAR
066-022-08002	AUD
	DKK

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Account	Currency
	EUR
	GBP
	JPY
	NOK
	SEK
	USD
066-022-08004	AUD
	BRL
	EUR
	GBP
	JPY
	PLN
	TRY
	TWD
	USD
	ZAR
066-022-07100	KRW
066-022-07101	KRW
066-022-07102	KRW
066-022-07107	KRW

Annex 2: Summary of the ETD Accounts

Account No.	Barclays POD (USD)	LBIE's current view of the potential Unsecured Claim value (USD)	LBIE's current view of the potential Client Money Claim (USD)
LBIE London			
066-022-07000	154,414,667	206,623,680	89,001,628
066-022-08001	-	(21,145,814)	8,520,024
066-022-08002	7,724,617	19,171,770	7,062,024
066-022-08000	702,094,032	631,166,203	783,224,296
066-022-07015	1,325,859	1,302,733	1,311,225
066-022-07003	-	(2,432,532)	(1,234,951)
066-022-08004	7,396,714	2,821,118	5,617,522
Sub-total:	872,955,889	837,507,158	893,501,767
LBIE Seoul			
071-022-07101	84,288,290	53,105,423	95,697,744
071-022-07107	28,698,853	22,299,288	33,043,335
071-022-07102	16,181,975	16,545,118	16,559,445
071-022-07100	664,458	679,369	679,957
Sub-total:	129,833,576	92,629,198	145,980,482
TOTAL:	1,002,789,465	930,136,356	1,039,482,249

Party: Applicant
Witness: R. Downs
Statement No: 10
Exhibit: "RD10"
Date: 5 September 2016

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

TENTH WITNESS STATEMENT OF
RUSSELL DOWNS

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Party: Applicant
Witness: R. Downs
Statement No: 10
Exhibit: "RD10"
Date: 5 September 2016

IN THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
COMPANIES COURT

No. 7942 of 2008

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

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

EXHIBIT "RD10" TO

THE TENTH WITNESS STATEMENT OF RUSSELL DOWNS

This is the exhibit marked "RD10" referred to in the Tenth Witness Statement of Russell Downs dated 5 September 2016.

Signed

