

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

ELEVENTH WITNESS STATEMENT
OF

RUSSELL DOWNS

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

- 1 I am a licensed insolvency practitioner and a partner in the firm of PwC of the above address. On 15 September 2008, Anthony Victor Lomas and Steven Anthony Pearson, on 2 November 2011, myself and on 22 March 2013, Julian Guy Parr, were appointed as joint administrators (the "**LBIE Administrators**") of Lehman Brothers International (Europe) (in administration) ("**LBIE**") pursuant to orders of the High Court, Chancery Division of England and Wales. I am duly authorised to make this statement on behalf of LBIE and the LBIE Administrators.
- 2 I make this statement in support of the LBIE Administrators' application for an order pursuant to paragraph 63 of Schedule B1 to the Insolvency Act 1986 (the "**Act**") for directions as described in section I below (the "**LBIE Application**") in respect of a settlement of the Waterfall III proceedings.

- 3 I have worked on the administration of LBIE (the "**LBIE Administration**") for more than six years and, as noted above, have been a LBIE Administrator for more than five years. In that time, I have been responsible for LBIE's affiliate relationships which have had a material impact on the success of the LBIE Administration, and since 2014 I have been responsible for all remaining counterparty activity as further progress was made to resolve creditors' claims not yet admitted for dividend by the LBIE Administrators.
- 4 This witness statement is made in support of the LBIE Application for directions that LBIE be at liberty to enter into a settlement with certain affiliated companies, the terms of which are described below.
- 5 I understand that the joint administrators of the LBIE UK affiliates set out below are also issuing applications pursuant to paragraph 63 of Schedule B1 to the Act for directions concerning matters related to the LBIE Application, with the intention that the Court hears the LBIE Application and the affiliates' respective applications together at the same hearing, in light of the inter-relationship between those applications and the proposed transaction they each contemplate:
- 5.1 the joint administrators of Lehman Brothers Limited (in administration) ("**LBL**") (the "**LBL Application**"); and
- 5.2 the joint administrators of LB Holdings Intermediate 2 Limited (in administration) ("**LBHI2**") (the "**LBHI2 Application**" and, together with the LBIE Application and the LBL Application, the "**Settlement Applications**").
- 6 In addition to LBL and LBHI2, two other Lehman UK affiliates will be parties to the proposed settlement, being:
- 6.1 Lehman Brothers Holdings plc (in administration) ("**LBH**"); and
- 6.2 Lehman Brothers Europe Limited ("**LBEL**"),
- (LBL, LBHI2, LBH and LBEL together being the "**Affiliates**"). I understand that the Administrators of LBH and LBEL also intend to attend the hearing of the Settlement Applications by counsel.
- 7 There is now produced and shown to me a paginated bundle of documents marked "**RD11**", to which I shall refer. Save where otherwise stated, page references in this witness statement are to the contents of RD11 which appears as an exhibit to this

witness statement. References to a “Rule” are to a rule provided for in the Insolvency Rules 1986 or the Insolvency (England and Wales) Rules 2016 (as applicable). References to a “Section” are to a section of the Act. Terms capitalised but not otherwise defined have the meaning given to them in the Application.

- 8 Save where otherwise stated, this witness statement is made from facts and matters that are within my own knowledge. Nothing that I say in this witness statement is intended to be a waiver of any privilege to which LBIE and/or the LBIE Administrators are entitled and no such privilege is waived.
- 9 The settlement terms and consequent applications for directions have been the subject of extensive correspondence and negotiations among LBIE, the Affiliates and Lehman Brothers Holdings, Inc (“LBHI”) (LBIE’s and the Affiliates’ ultimate parent which has a material direct and indirect economic interest in the Affiliates), since December 2016.
- 10 As described in further detail below, the LBIE Administrators believe that the proposed settlement of LBIE’s relationships with its shareholders is both something that is within their statutory powers and would result in a beneficial outcome for the LBIE Administration and involve a timely and appropriate exercise of their duties in the interests of LBIE’s creditors as a whole. However, the LBIE Administrators consider the settlement – particularly in the context of the wider UK Lehman group insolvency processes – to be a matter of sufficient significance such as to make it appropriate for them to seek an Order from the Court that they be at liberty to enter into it.
- 11 I have been shown an advanced draft of the Fifth Witness Statement of Gillian Eleanor Bruce, which sets out a summary of the proposed settlement and its key terms. I do not repeat such summary in this statement, and am making this witness statement to provide the Court with relevant supplementary material related to the LBIE Administration.
- 12 Relatively late in the process of negotiating the settlement, an issue was identified relating to a claim that might be made against certain of the Affiliates. LBIE and the other parties to the proposed settlement are currently in discussions as to how that ought to be dealt with as part of the proposed settlement. In order to proceed with the settlement, it will need to be resolved satisfactorily from the point of view of the LBIE Administrators. What follows in this witness statement proceeds on the basis

that it will be satisfactorily resolved. The LBIE Administrators will of course update the Court in this regard as appropriate ahead of and/or at the hearing of the Settlement Applications.

- 13 The remainder of this witness statement is divided into the following nine sections:
 - 13.1 Section A: Background
 - 13.2 Section B: Status of the LBIE Surplus
 - 13.3 Section C: Claims Between LBIE and the Affiliates
 - 13.4 Section D: The Waterfall I Application
 - 13.5 Section E: The Waterfall II Application
 - 13.6 Section F: The Waterfall III Application
 - 13.7 Section G: The Administrators' Assessment of the Backstop 2 Arrangement (as defined in paragraph 43)
 - 13.8 Section H: Engagement with LBIE Creditors
 - 13.9 Section I: The Proposed Directions

A. BACKGROUND

- 14 As is now well known, LBIE was the principal trading company within the European group of Lehman Brothers companies and is an English unlimited company. LBIE was authorised and regulated by the Financial Services Authority (now called the Financial Conduct Authority). According to filings made at Companies House and LBIE's share register, LBL and LBHI2 are the only shareholders of LBIE (the "**Members**"). LBL owns one ordinary share of \$1. LBHI2 owns:
 - 14.1 2 million 5% redeemable Class A preference shares of \$1000 each;
 - 14.2 5.1 million 5% redeemable Class B shares of \$1000 each; and
 - 14.3 6,273,113,999 ordinary shares of \$1 each in LBIE.
- 15 LBIE entered into administration (the "**Administration**") on 15 September 2008 (the "**Administration Date**").

- 16 On 2 December 2009, the High Court of Justice made an order granting permission for the LBIE Administrators to make a distribution to creditors and on 4 December 2009 the LBIE Administrators gave notice to creditors pursuant to Rule 2.95 of their intention to distribute. Following three interim distributions, on 30 April 2014, the LBIE Administrators paid a final, fourth interim dividend in respect of the proved claims (as at that date) of unsecured creditors, which took the aggregate dividends paid to LBIE's general unsecured creditors with proved claims to 100 pence in the pound in respect of such claims. Admitted claims amount to approximately £12.3bn. There is a surplus in LBIE's estate after the payment in full of the proved claims of all general unsecured creditors admitted for dividend (the "**Surplus**").
- 17 The LBIE Administrators' Seventeenth progress report dated 10 April 2017 (for the period 15 September 2016 to 14 March 2017) (the "**LBIE Progress Report**") shows cash and cash equivalent balances (after having paid admitted claims in full) of £6.58bn and estimates that, subject to a number of important assumptions, the Surplus will ultimately be between c.£7.04bn (in a low case scenario) and c.£8.19bn (in a high case scenario). The LBIE Progress Report is at **pages 1 to 38**.
- 18 However, as explained further in this statement, there remain (albeit, for reasons explained in this witness statement, unlikely) scenarios in which the claims for post-administration interest, non-provable claims and subordinated debt claims against LBIE in respect of the Surplus might exceed the amount of the Surplus. If that were to happen and if (which is also presently unlikely) LBIE were then to go into liquidation, there would at that stage be claims against its Members, LBHI2 and LBL, for a contribution to LBIE's assets under Section 74 in respect of those non-provable and subordinated debt claims ("**Contribution Claims**").
- 19 Information in relation to the Affiliates and the status of their respective administrations can be found at Appendix 1.
- 20 In addition to the substantial sums of cash and cash equivalents held in the LBIE estate noted above:
- 20.1 according to the LBL Administrators' latest progress report (for the period 15 September 2016 to 14 March 2017) (the "**LBL Progress Report**"), LBL holds £390m having paid only £1.8m to unsecured creditors.;

- 20.2 according to the LBHI2 Administrators' latest progress report (for the period 14 July 2016 to 13 January 2017) (the "**LBHI2 Progress Report**"), LBHI2 holds £704m having made no distributions to unsecured creditors.;
- 20.3 according to the LBH Administrators' latest progress report (for the period 15 September 2016 to 14 March 2017) (the "**LBH Progress Report**"), LBH holds £63m having made distributions to creditors of £63m. A copy of the LBH Progress Report is at **pages 39 to 55**; and
- 20.4 according to the LBEL Administrators' latest progress report (for the period 23 September 2016 to 22 March 2017) (the "**LBEL Progress Report**"), LBEL holds £277m after having paid admitted creditor claims in full. A copy of the LBEL Progress Report is at **pages 56 to 71**.

Further information in relation to the Affiliates' estates can be found at Appendix 1.

- 21 As a result of the interrelationships among LBIE and the Affiliates described below and various legal uncertainties and/or disputes, and in particular the proof of debt filed by LBIE against LBL (in the amount of c.£10.4bn) and the statement of claim delivered by LBIE to LBHI2 (in the amount of c.£10bn), further distributions have not been possible in the Affiliates' estates until a resolution is obtained in relation to some or all of the matters addressed in the Waterfall I Application, the Waterfall II Application and the Waterfall III Application (discussed at sections D-F below), because very high reserves have needed to be maintained in respect of these claims. This impediment to further distributions was further compounded by the fact that the majority of the estate balances of LBEL and LBH would, once distributed, flow to LBL in the first instance where they would again be trapped in LBL's estate to the extent that the LBL Administrators were unable to make distributions. The Affiliates also have claims among themselves.
- 22 From the start of 2017, LBIE, LBHI and the Affiliates redoubled efforts to explore the basis of a settlement of the Waterfall III Application. In taking this course, the Affiliates were motivated by a desire to accelerate their ability to make the long-delayed distributions. The LBIE Administrators themselves were motivated by a desire to advance the time at which one of the more significant outstanding issues in the LBIE estate could be resolved. Such settlement discussions were premised upon the law as it then stood prior to the Supreme Court judgment in the Waterfall I Application. Such efforts resulted in agreement on an outline transaction, details of which were

published on the LBIE Administration section of the PwC website (the “**Website**”) on 29 March 2017 (a copy of that announcement is at **pages 72 to 75**). However, certain aspects of the Supreme Court judgment in the Waterfall I Application (as to which see paragraphs 31 and 32 below) materially altered certain of the Affiliates’ assessment of the proposed transaction such that they sought fundamentally to revise its terms.

- 23 The judgment of the Supreme Court in the Waterfall I Application has significantly reduced the legal uncertainties affecting the position among LBIE and the Affiliates. In light of this, the settlement now proposed would, by resolving further legal issues in relation to the Surplus, facilitate further distributions by and among the Affiliates.

B. STATUS OF THE LBIE SURPLUS

- 24 As explained above at paragraph 17, the Surplus is estimated in the LBIE Progress Report to be in a range between c.£7.04bn in a low case and c.£8.19bn in a high case. On 30 April 2014, LBIE paid its final interim dividend on unsecured debts proved as at that date. Claims agreed after that date have been paid in full upon finalisation of such agreement. The LBIE Administrators have, as yet, been unable to make any distributions from the Surplus. Accordingly, three years have now passed without any distribution having been made to LBIE's creditors from the Surplus.
- 25 As regards the claims in respect of the Surplus, these can be summarised as follows (listed in order of priority ranking, as to which see paragraph 32.1 below):
- 25.1 interest on proved debts payable pursuant to (what was) Rule 2.88(7) (“**Statutory Interest**);
 - 25.2 certain potential non-provable claims which are (amongst other things) the subject of the Waterfall II Application (“**Non-Provable Claims**” and, together with Statutory Interest, “**Senior Creditor Entitlements**”); and
 - 25.3 an unsecured subordinated claim in respect of sums advanced to LBIE under three subordinated debt agreements dated 1 November 2006 in the amount of around £1.254bn (the “**Sub-Debt**”).

- 26 The principal reasons for the LBIE Administrators' inability, to date, to make distributions from the Surplus are as follows:
- 26.1 the need to reserve for certain claims;
 - 26.2 the complexities associated with reserving on an appropriately conservative basis for claims to Statutory Interest at a rate exceeding the Judgments Act rate (given the ongoing proceedings in that regard, as to which see section E below); and
 - 26.3 the inability of the stakeholder community to reach a consensus to support a proposal to facilitate interim distributions from the Surplus.
- 27 The LBIE Administrators have, over the past several years, sought resolution of the issues relating to those claims, their inter-relationship and various related issues, in particular through what are known as the "Waterfall" applications to Court for directions pursuant to paragraph 63 of Schedule B1 to the Act. The issues with which those applications are concerned, and their procedural progress, are summarised at sections D-F below. In parallel, the LBIE Administrators have sought, as appropriate, to encourage consensus among LBIE's key stakeholders, but to date such efforts have not been successful.

C. CLAIMS AMONG LBIE AND THE AFFILIATES

- 28 LBIE and the Affiliates have identified numerous, substantial and (in some cases) overlapping claims and potential claims against each other. Certain of these claims are subject to the Waterfall proceedings, insofar as such proceedings will determine (or have now determined) or impact (inter alia):
- 28.1 the existence of such claims;
 - 28.2 the circumstances in which such claims may be brought;
 - 28.3 the quantum of such claims;
 - 28.4 the availability of set-off in respect of, or between, such claims; and/or
 - 28.5 the assets available to meet such claims.
- 29 The claims asserted between LBIE and the Affiliates are further described at Appendix 4 to this witness statement.

D. THE WATERFALL I APPLICATION

30 On 14 February 2013, the LBIE Administrators, together with the respective administrators of LBL and LBHI2, issued the first Waterfall Application ("**Waterfall I**"). A description of the issues with which Waterfall I is concerned, and the procedural history of the Waterfall I Application, can be found at Appendix 2, but in brief these relate to:

- 30.1 the priority ranking of the Sub-Debt for payment from the Surplus;
- 30.2 the existence of Currency Conversion Claims (a non-provable claim in relation to foreign currency debts, arising from the diminution in value of sterling between the date of administration (on which foreign currency debts are converted into sterling for the purpose of proof), and the date(s) on which sterling dividends are paid in respect of such debts); and
- 30.3 the scope of Contribution Claims and the circumstances in which they may be brought.

31 On 17 May 2017, the Supreme Court handed down its judgment in the Waterfall I Application (the "**SC Judgment**"). A copy of the SC Judgment is at **pages 76 to 148** and a copy of the Supreme Court's press summary of its conclusions is at **pages 149 to 151**.

32 The Supreme Court reached certain conclusions which are of particular significance for present purposes. Specifically, the Supreme Court:

- 32.1 confirmed that the Sub-Debt ranks for payment behind Statutory Interest and Non-Provable Claims;
- 32.2 held (overturning the judgments of David Richards J and the Court of Appeal) that Currency Conversion Claims do not exist;
- 32.3 held (overturning the judgments of David Richards J and the Court of Appeal) that LBIE in administration cannot prove in the administration or liquidation of its Members in respect of a future Contribution Claim;
- 32.4 held (overturning the judgments of David Richards J and the Court of Appeal) that LBIE cannot make a Contribution Claim in order to allow it to pay Statutory Interest;

- 32.5 held (overturning the judgment of the Court of Appeal) that Statutory Interest accrued but unpaid in an administration is not payable in any subsequent liquidation; and
 - 32.6 held (overturning the judgments of David Richards J and the Court of Appeal) that the contributory rule applies in a distributing administration, such as to prevent the Members being paid on their proofs in the LBIE administration until they have discharged any potential liability under Section 74.
- 33 Having considered the judgment fully, the LBIE Administrators consider that the effect of the SC Judgment is to reduce significantly the likelihood of a Contribution Claim arising. Specifically:
- 33.1 confirmation that the Sub-Debt ranks for payment behind Statutory Interest and Non-Provable Claims reduces the likelihood of there being a shortfall in LBIE's ability to meet Senior Creditor Entitlements from its own resources;
 - 33.2 the decision that Currency Conversion Claims do not exist as a species of Non-Provable Claim has reduced the quantum of Senior Creditor Entitlements by approximately £2.5bn (including interest potentially payable thereon);
 - 33.3 the decision that LBIE in administration cannot prove in the administration or liquidation of its Members in respect of a future Contribution Claim means that LBIE would have to move into liquidation in order to make a Contribution Claim, such that no party can presently make a Contribution Claim (even if one might arise in the future);
 - 33.4 the decision that LBIE cannot make a Contribution Claim in order to allow it to pay Statutory Interest means that a Contribution Claim (and moving into liquidation in order to pursue it) would only be necessary to the extent that there is a shortfall in LBIE's ability to pay Non-Provable Claims (which, as noted above at 32.2, do not include Currency Conversion Claims) or (subject to the outcome of certain issues in the Waterfall III proceedings) the Sub-Debt;
 - 33.5 the decision that Statutory Interest accrued but unpaid in an administration is not payable in any subsequent liquidation means that any move into liquidation prior to the payment of accrued Statutory Interest would result in

creditors not being paid such Statutory Interest. This is a significant reason why the LBIE Administrators have taken the view that for LBIE to go into liquidation prior to payment of Statutory Interest to which LBIE's creditors are entitled in the LBIE Administration would not be in the interests of LBIE's creditors as a whole.

- 34 Accordingly, the overall effect of the SC Judgment is to:
- 34.1 limit the circumstances in which LBIE could bring a Contribution Claim (none can presently be brought);
 - 34.2 reduce the economic circumstances in which LBIE might otherwise be able to bring a Contribution Claim;
 - 34.3 reduce the likely necessity for bringing a Contribution Claim; and
 - 34.4 introduce a real economic disadvantage to LBIE's creditors as a whole were LBIE to go into liquidation so that a Contribution Claim might be made.

E. THE WATERFALL II APPLICATION

- 35 On 12 June 2014, the LBIE Administrators issued the Waterfall II Application ("**Waterfall II**"). A description of the issues with which Waterfall II is concerned, and the procedural progress of the application, can be found at Appendix 3, but in brief these relate to:
- 35.1 how Statutory Interest on admitted claims is to be calculated;
 - 35.2 how Currency Conversion Claims are to be calculated;
 - 35.3 the date from which Statutory Interest is to run in respect of contingent and future debts;
 - 35.4 how interest claims under ISDA Master Agreements (and similar agreements) are to be quantified; and
 - 35.5 the impact on claims to Statutory Interest and/or Currency Conversion Claims of releases contained in certain post-administration contracts.

- 36 For present purposes, and following the SC Judgment (including its conclusion that there are no Currency Conversion Claims), the significance of the Waterfall II Application is primarily in determining:
- 36.1 the quantum of the Statutory Interest payable in the LBIE Administration. This will depend on the following issues:
- 36.1.1 whether Statutory Interest is to be calculated on the basis that dividends are to be treated as having been allocated first to the payment of accrued Statutory Interest (the “**Bower v Marris**” basis) or first to the reduction of principal; and
- 36.1.2 how default rates of interest are to be calculated under ISDA Master Agreements and other similar agreements; and
- 36.2 whether certain Non-Provable Claims (relating to the payment of Statutory Interest) exist, namely:
- 36.2.1 a claim in respect of the continued compounding of interest on a contractual basis following the payment in full of the principal amount of the debt; and
- 36.2.2 a claim in respect of delay in payment of Statutory Interest (on a *Sempra Metals* basis). The parties arguing for the existence of such a claim have not explained precisely how such a claim would fall to be calculated.
- 37 The Waterfall II Application is currently the subject of appeals to the Court of Appeal.

F. THE WATERFALL III APPLICATION

- 38 In summary, the Waterfall III application seeks directions from the Court in relation to the following matters:
- 38.1 whether the obligations of LBHI2 and LBL to contribute to the assets of LBIE under Section 74 extend to a contribution to enable LBIE to pay the Sub-Debt, and if so:
- 38.1.1 how that claim is to be valued; and
- 38.1.2 whether and how such claim is impacted by insolvency set-off;

- 38.2 the rights *inter se* of LBHI2 and LBL in respect of any obligation to contribute to the assets of LBIE under Section 74;
- 38.3 whether LBL is properly to be treated as a shareholder of LBIE with a potential obligation to contribute to the assets of LBIE under Section 74; and
- 38.4 whether LBL is entitled to recharge to any or all of the Affiliates certain sums, including sums payable to LBIE under Section 74.
- 39 The full set of issues in the Waterfall III application are set out at Appendix 5.
- 40 For case management purposes, the Waterfall III application was split into two parts, as follows:
- 40.1 Part A of the application deals with purely legal (i.e. non-fact dependent) issues. Those are Issues 1 to 8, 9A, 10 and 12, as set out in Appendix 5. Part A was heard by Mr Justice Hildyard at a hearing commenced on 30 January 2017. However, the Judge indicated (further to a request by the parties) that:
- 40.1.1 he would not hand down judgment in respect of Part A until the Supreme Court hands down its judgment in respect of Waterfall I, on the basis that the Supreme Court's decision might impact on the analysis applicable to certain Part A issues; and
- 40.1.2 he might require further submissions in respect of the Part A issues in light of the Supreme Court's judgment in Waterfall I;
- 40.2 Part B of the application deals with issues of fact, being Issues 9, 11, 13 and 14, as set out in Appendix 5. Of those issues:
- 40.2.1 Issues 9 and 11 are due to be heard by Mr Justice Hildyard at a hearing listed to commence on 11 September 2017 and last for eleven days; and
- 40.2.2 Issues 13 and 14 have, in light of the SC Judgment, been adjourned following a hearing before Mr Justice Hildyard on 19 June 2017.
- 41 Whilst it is difficult to predict the course that any given piece of litigation will take (and leaving aside their views as to the merits of the various issues), the LBIE Administrators' experience of the various Waterfall proceedings (and other litigation in the LBIE Administration) to date suggests that, in light the complexity of the issues, the sums of money involved and the potential impact of the Court's directions on

LBIE's creditors and, in particular, those of the Affiliates, parties to the application are likely to seek permission to appeal at least some of the issues in Waterfall III and the application may well only be finally determined (at least in some respects) by the Supreme Court. Based, again, on their experience of the proceedings to date in the LBIE Administration, the LBIE Administrators estimate that the issues in Waterfall III, insofar as they progressed on appeal to the Supreme Court, may not be fully determined until some point in 2021 or later.

- 42 In light of the possibility of such protracted litigation, LBIE, the Affiliates and LBHI have reached agreement as part of the broader Backstop 2 Arrangement, subject to the Court's granting of the directions sought, on a resolution of the issues in Waterfall III which would avoid such litigation and advance the interests of their respective creditors.

G. THE ADMINISTRATORS' ASSESSMENT OF THE BACKSTOP 2 ARRANGEMENT

- 43 The proposed backstop arrangement is summarised in the Fifth Witness Statement of Gillian Eleanor Bruce and filed on behalf of the joint administrators of LBHI2 (the "**Backstop 2 Arrangement**"). The Backstop 2 Arrangement will be given effect by the following documents:

- (a) Deed of Settlement;
- (b) Inter-affiliate Distribution Deed;
- (c) Master Framework Agreement;
- (d) Limited Recourse Deed; and
- (e) an Indemnity between LBHI and LBIE,

(together the "**Transaction Documents**" and each a "**Transaction Document**"). The Transaction Documents are exhibited to Ms Bruce's witness statement.

- 44 As will be apparent from the summary at section F above, the Waterfall III Application was predicated to a significant extent upon the real possibility of LBIE being in a position – and it being in the interests of LBIE's creditors – to bring Contribution Claims against its Members. As explained above at 33.3, LBIE in administration and the LBIE Administrators have no standing to make a Contribution Claim, and the

LBIE Administrators consider that, even if LBIE were to move into liquidation, it is most unlikely that Contribution Claims would be necessary. The Administrators' assessment of the Backstop 2 Arrangement is made in that context.

- 45 The LBIE Administrators understand the desire of the administrators of the Affiliates to progress their estates and, critically, to find an accelerated basis upon which distributions can be made from their aggregated £1.4bn of net realisations. Following the judgment of the Supreme Court in the Waterfall I Application, the LBIE Administrators currently have no basis upon which to object to such distributions being made.
- 46 The LBIE Administrators have considered and dismissed the possibility of moving LBIE into liquidation in order to protect LBIE's ability to make Contribution Claims in the unlikely event that there is value in such claims in due course.
- 47 Accordingly, the LBIE Administrators have engaged in these settlement discussions with a view to securing as favourable an outcome as possible, recognising that LBIE and the LBIE Administrators have no standing to object to the Members making distributions without making provision for any Contribution Claim. The LBIE Administrators consider that this approach has been successful based on the benefits achieved and noted below.
- 48 The Administrators consider that the Backstop 2 Arrangement provides benefits (outlined in paragraphs 49 to 53 below) to LBIE such that it is in the interests of LBIE's creditors as a whole for the Administrators to enter into it.
- 49 First, Wentworth's agreement to waive any right be paid the Sub-Debt from anything other than LBIE's existing assets effectively caps LBIE's liability in respect of the Sub-Debt and, by removing the possibility of a Sub-Debt Contribution Claim, brings forward the point at which LBIE has certainty in respect of the Sub-Debt claim and means that the majority of the Waterfall IIIA issues do not require resolution.
- 50 Secondly, by agreeing with LBL a nil balance in respect of LBIE and LBL's claims against each other, LBIE will avoid the further costs of dealing with LBL's claims (including costs in relation to disputed proofs) and any balance in favour of LBL that might be determined.
- 51 Thirdly, the settlement of the Waterfall III proceedings will:

- 51.1 remove the possibility of – and the need to reserve for – LBL’s recharge claims. The quantum of those claims (excluding the recharge of any Contribution Claim) is significant (some £934.6 million on their face, as claimed by LBL);
- 51.2 resolve and/or avoid the need to resolve the legal uncertainty that presently arises in respect of the issues in Waterfall III and which would, absent settlement, require resolution in order for the administration of LBIE’s estate to be completed;
- 51.3 avoid further substantial costs being incurred by LBIE in respect of the proceedings, including:
 - 51.3.1 in respect of those issues which are currently adjourned (see paragraph 40.2.2 above); and
 - 51.3.2 on appeals which, given the progress of the other Waterfall proceedings to date, would appear likely.
- 52 Fourthly, LBIE will obtain an indemnity from LBHI, capped at £62 million, to cover any shortfall in LBIE’s ability to pay Senior Creditor Entitlements, including Statutory Interest accrued in the LBIE Administration. The cap of £62 million reflects the sum which LBIE considers it is owed by LBL but in respect of which it is agreeing a nil balance.
- 53 Fifthly, by facilitating the making of further distributions from the estate of LBH plc, the settlement will expedite further distributions by LBH plc on LBIE’s admitted claim of approximately £38 million.
- 54 In return for these benefits, the LBIE Administrators will:
 - 54.1 agree not to object to its Members making certain distributions without reserving for any future Contribution Claim. The LBIE Administrators consider this to be a reasonable step in circumstances where they have concluded that they have no reasonable basis for such an objection in any event given:
 - 54.1.1 that LBIE in administration and the LBIE Administrators have no standing to make a Contribution Claim;

- 54.1.2 the size of the Surplus and the quantum of the likely claims against it mean that (as matters stand) no Contribution Claim would presently arise even if LBIE were in liquidation; and
 - 54.1.3 it appears most unlikely that LBIE will ever have any need to make a Contribution Claim; and
- 54.2 acquiesce in the transfer to LBHI2 of LBL's share in LBIE, taking only such positive steps as are required of them under the Companies Act 2006. Again, the LBIE Administrators consider this to be a reasonable approach in circumstances where they have concluded that there would be no sensible basis for seeking to obstruct such transfer; indeed, the Members can effectively take the relevant steps without any involvement from LBIE or the LBIE Administrators.
- 55 As regards agreeing not to object to LBIE's Members making certain distributions without reserving for any future Contribution Claims, it is important to emphasise that, in reality, this is not a material concession, for the reasons set out below.
- 56 Further to the SC Judgment, LBIE in administration and the LBIE Administrators have no standing to object to the Members making certain distributions without reserving for any future Contribution Claims. The only circumstance in which LBIE would be able to object to LBIE's Members making such distributions without reserving for any future Contribution Claim is where LBIE has moved into liquidation.
- 57 However, as touched on above it will be very difficult, for various reasons, to justify moving LBIE into liquidation. In particular:
 - 57.1 in light of the SC Judgment, it will be very difficult to justify moving LBIE into liquidation prior to payment of Statutory Interest to which LBIE's creditors are entitled in the LBIE Administration, given that any such move into liquidation would have the effect of bringing that Statutory Interest entitlement to an end; and
 - 57.2 furthermore, entry into liquidation would attract certain negative tax consequences, including:
 - 57.2.1 liquidation would break the tax group of which LBIE is a part, leading to fewer opportunities to use Group relief to shelter losses going

forward, in particular to shelter profits made on LBIE's investment income;

57.2.2 liquidation would also terminate the VAT group of which LBIE is a part. The recovery rate applicable to LBIE would then need to be negotiated with HMRC and could well be lower than the rates currently applicable;

57.2.3 the date of liquidation would be taken as the date LBIE ceased to trade, which may have a further impact on LBIE's tax position; and

57.2.4 liquidation creates a new tax period for LBIE.

58 Moreover, even if LBIE were to move into liquidation such that its liquidator would have standing to make a Contribution Claim, it is very possible (if not probable) that any Contribution Claim would have no value in any event. In particular, given the current estimated size of the Surplus and the fact that a Contribution Claim cannot be made in respect of Statutory Interest, the LBIE Administrators consider that the only circumstances in which a Contribution Claim might have any value would be where, contrary to the current law:

58.1 there are held to be Non-Provable Claims. As to this, there would need to be a successful (and final) appeal establishing a non-provable claim:

58.1.1 to damages on the *Sempra Metals* basis; and/or

58.1.2 in respect of the continued compounding of interest on a contractual basis following the payment in full of the principal amount of the debt;

and

58.2 either:

58.2.1 there was a successful (and final) appeal on the *Bower v Marris* issue in Waterfall IIA; and/or

58.2.2 there was a successful (and final) appeal on the cost of funding issues in Waterfall IIC.

59 For these reasons, the LBIE Administrators consider that the giving up of the possibility of objecting to LBIE's Members making distributions without reserving for any future Contribution Claim does not, for all practical purposes, represent a

material (if any) concession. It should also be noted that the LBIE Administrators are not conceding any right they or LBIE might have to object to subsequent distributions, albeit there of course will, in the event that the transaction contemplated is completed, be much more limited funds in the estate of LBHI2 (which might be the sole remaining Member) by the time any objection could sensibly be made.

- 60 Having given careful consideration to all of these matters, and having concluded the relevant negotiations with the other parties to the proposed settlement, the LBIE Administrators are satisfied that the advantages of this settlement outweigh any disadvantages and that this settlement is in the interests of LBIE's creditors as a whole. In particular, given that the crucial potential "disadvantage" identified above (i.e. the giving up of the possibility of LBIE Administrators' objecting to LBIE's Members making distributions without reserving for any future Contribution Claims) is to a large extent an illusory one, the LBIE Administrators consider that the proposed settlement is plainly in the interests of LBIE's creditors as a whole. I should add that I am the only one of the LBIE Administrators who is not also an administrator of one or more of the Affiliates who are the other parties to the Backstop 2 Arrangement. As stated above, I have had primary responsibility for all affiliate relationships and as such took on the negotiation of the proposed settlement. I have satisfied myself that in making the decision to enter into this settlement, I have been able to consider the best interest of LBIE and its creditors as a whole without regard to the interests of the other Lehman group parties.

H. ENGAGEMENT WITH LBIE CREDITORS

- 61 Broadly speaking, LBIE's unsecured, unsubordinated creditor population can be summarised as follows:

61.1 the "Senior Creditor Group" comprised of:

61.1.1 Burlington Loan Management Limited

61.1.2 CVI GVF (Lux) Master S.à.r.l.; and

61.1.3 Hutchinson Investors, LLC (the "**SCG**").

61.2 Wentworth Senior (as defined at paragraph 9.1 of Appendix 4); and

61.3 other creditors.

- 62 The breakdown of unsecured claims among those groups of creditors is as follows:

Creditor	Claim value (£m)	Percentage
Wentworth and Affiliates	4.9	40
SCG	4.5	37
Others	2.9	23
	12.3	100

- 63 Throughout the LBIE Administration, the LBIE Administrators have used postings on the Website to make key announcements and documents available to LBIE's creditors. This has been the case particularly in relation to the various Waterfall proceedings given their impact upon creditors' entitlements in respect of the Surplus.
- 64 In relation to the present Application, the LBIE Administrators have communicated with LBIE's creditors as a whole by way of updates on the Website in the usual way.
- 65 In particular, and as noted above at paragraph 22, on 29 March 2017, the LBIE Administrators posted an announcement to the Website which provided LBIE's creditors with a detailed summary introduction to the proposed terms of a settlement of the Waterfall III proceedings. The announcement also provided contact details for LBIE's Communications and Counterparty Management team for LBIE creditors to send any questions or feedback in respect of the announcement. A copy of the announcement is at **pages 72 to 75**.
- 66 In the LBIE Progress Report, published on 10 April 2017, the LBIE Administrators explained that LBIE was exploring a *"multi-Affiliate settlement which would enable the Waterfall III legal proceedings to end"*. A copy of the LBIE Progress Report is at **1 to 38**.
- 67 On 23 June 2017, the LBIE Administrators posted a further announcement to the Website indicating, amongst other things, that following the SC Judgment:
- 67.1 there was no longer appetite among the interested parties for a transaction in the form outlined in the Administrators' update of 29 March 2017; and
- 67.2 the interested parties had recently resumed discussions in relation to a possible revised transaction involving the withdrawal of Contribution Claims and a conclusion of the Waterfall III proceedings.

A copy of the announcement is at **pages 152 to 155**.

- 68 On 12 July 2017, the LBIE Administrators posted an announcement to the Website which provided LBIE's creditors with a detailed summary of the proposed terms of the Backstop 2 Arrangement. The announcement also provided contact details for LBIE's Communications and Counterparty Management team for LBIE creditors to send any questions or feedback in respect of the announcement. The announcement was updated on 13 July 2017 to inform creditors of the date for the hearing of the LBIE Application. A copy of the announcement is at **pages 156 to 157**.
- 69 On 18 July 2017, the LBIE Administrators emailed representatives of the SCG, indicating that the LBIE Administrators were preparing for the hearing of this application and requesting that the SCG provide by return any feedback it had in relation to the proposed settlement. I had previously spoken to representatives of the SCG, among other things, about the developing proposed settlement.
- 70 At the date of this witness statement, the LBIE Administrators are aware of one query that has been raised in relation to one aspect of the deal. An exchange of emails relating to that query is at **pages 158 to 162**. The LBIE Administrators also received a question from one of LBIE's affiliate creditors relating not directly to the proposed settlement but to the LBIE Administrators' views in respect of the Statutory Interest "lacuna". The email exchange in that regard is at **pages 163 to 165**. Those queries aside, the LBIE Administrators have not received any feedback in relation to the Backstop 2 Arrangement and have not received any expressions of concern or points that cause them to alter their view as to the merits of the settlement from the point of view of LBIE and its creditors.
- 71 The LBIE Administrators intend to post the LBIE Application and this witness statement on the Website ahead of the hearing to ensure that, taking into account the updates and announcements and other engagement with them, LBIE's creditors have seen sufficient relevant information to have raised concerns or objections if they had any.

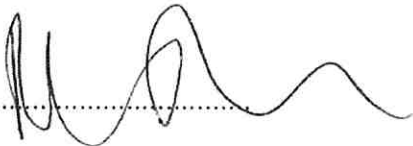
I. THE PROPOSED DIRECTIONS

- 72 The LBIE Administrators do not request the Court's specific determination that they should enter into the proposed settlement. However, having satisfied themselves that the proposed settlement is in the best interests of LBIE's creditors as a whole,

they do request the Court's permission to enter into the proposed settlement on the basis that such a direction is appropriate given its significance to the LBIE Administrators generally and the fact that it resolves outstanding issues among a number of affiliated estates. The LBIE Administrators request that the Court makes an order directing that the LBIE Administrators be at liberty to cause LBIE to enter into and execute the Transaction Documents in order to implement the Backstop 2 Arrangement.

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

Dated 20 July 2017

A handwritten signature in black ink, consisting of a series of loops and a long horizontal stroke, positioned above a dotted line.

Russell Downs

Party: Applicant
Witness: Russell Downs
Statement No: 11
Exhibit: "RD11"
Date: 20 July 2017

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 "RD11" TO
NINTH WITNESS STATEMENT OF RUSSELL DOWNS

This is the exhibit marked "RD11" referred to in the Ninth Witness Statement of Russell Downs dated 20 July 2017.

Signed  ,

Party: Applicant
Witness: Russell Downs
Statement No: 11
Exhibit: "RD11"
Date: 20 July 2017

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

NINTH WITNESS STATEMENT
OF
RUSSELL DOWNS

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Solicitors for the Claimant

Ref: Tony Bugg/Euan Clarke/Jared Oyston

Appendix 1: Information in relation to the Affiliates

LBL

- 1 LBL is an English limited company. It is a shareholder of LBIE as set out at paragraph 14 above. It was the service company for the operations of the Lehman Brothers group of companies in the UK, Europe and Middle East, holding most of the service contracts and employee contracts for UK companies within the Lehman Brothers group as well as buying in services specifically for other affiliates. LBL also maintained IT systems and provided infrastructure support to the European group of Lehman Brothers companies. Furthermore, LBL was the head lessee for the Lehman Brothers group's European headquarters at 25 Bank Street, London, as well as the "Group Paying Agent" for UK corporation tax, the "Representative Member" for the Lehman Group VAT registration, and the "Principal Employer" under the Lehman Brothers UK Pension Scheme. LBL also provided a payroll service in relation to LBL employees seconded to other Lehman Brothers group companies and an invoice payment service (such payroll costs and invoices themselves were recharged by LBL to the relevant Lehman Brothers group company at cost).
- 2 LBL entered into administration on 15 September 2008. LBL's current administrators are Michael John Andrew Jervis and Zelf Hussain (the "**LBL Administrators**"). On 20 June 2014, the High Court of Justice made an order granting permission for the LBL Administrators to make a distribution to creditors, and on 8 July 2014 the LBL Administrators gave notice to creditors pursuant to Rule 2.95 of their intention to distribute.
- 3 According to the LBL Progress Report dated 7 April 2017, the LBL Administrators have paid a dividend of 100 pence in the pound to former employees with preferential unsecured claims (comprising claims for unpaid wages and holiday pay) and a first interim dividend in December 2014 of 1.66 pence in the pound to ordinary unsecured creditors with proved claims.

LBHI2

- 4 LBHI2 is an English limited company. It is an intermediate holding company which holds shares in LBIE as set out at paragraph 14 above. LBHI2 was the immediate lender to LBIE of certain subordinated debt. LBHI2 had no other business of which I am aware.

- 5 LBHI2 entered into administration on 14 January 2009. Its current administrators are Anthony Victor Lomas, Steven Anthony Pearson, Derek Anthony Howell, Julian Guy Parr and Gillian Bruce (the "**LBHI2 Administrators**"). On 15 June 2017, the LBHI2 Administrators obtained permission to make interim distributions to unsecured creditors, subject to certain requirements to notify the LBIE Administrators such before filing a notice of intended distribution.
- 6 LBHI2 is also a participant in the Wentworth group of investors in LBIE unsecured debt, subordinated debt and equity.

LBEL

- 7 LBEL is an English limited company. LBEL's principal activity was the provision of investment banking and corporate finance services. It also arranged derivatives transactions as agent for other Lehman Brothers companies. It used employees seconded from LBL and was authorised and regulated by the Financial Services Authority (currently known as the Financial Conduct Authority).
- 8 LBEL entered into administration on 23 September 2008. Its current administrators are Dan Yoram Schwarzmann, Anthony Victor Lomas, Steven Anthony Pearson and Julian Guy Parr (the "**LBEL Administrators**"). On 25 June 2012, the High Court of Justice made an order granting permission for the LBEL Administrators to make a distribution to creditors and on 11 July 2012 the LBEL Administrators gave notice to creditors pursuant to Rule 2.95 of their intention to distribute. On 23 September 2014, the LBEL Administrators paid a third, final interim dividend in respect of the proved claims of unsecured creditors, which took the aggregate dividends paid to LBEL's general unsecured creditors with proved claims to 100 pence in the pound in respect of such claims. The LBEL Progress Report dated 20 April 2017 is at pages **56 to 71**.
- 9 On 16 May 2017, the LBEL Administrators filed an application to the High Court for directions as to the method or methods by which distributions to LBEL's sole shareholder, LBH plc, might permissibly be made.
- 10 The first hearing of the LBEL Administrators' application took place on 19 May 2017. On that occasion, the Court adjourned the matter and directed that LBEL Administrators, in advance of the next hearing, to give specific notice of the application to Her Majesty's Revenue and Customs ("**HMRC**").

- 11 On 15 June 2017, the application was further adjourned, by consent of the LBEL Administrators and HMRC, as the latter required more time to consider the proposed methods of distribution canvassed in the LBEL Administrators' application.
- 12 On 28 June 2017, HMRC sent a letter to the LBEL Administrators, confirming that it had no preference as between the various proposed methods of distribution canvassed in the LBEL Administrators' application. The letter was provided to the Court on 29 June 2017.
- 13 On 11 July 2017, the LBEL Administrators' application came before the Court again, but was adjourned in order for the positions of LBH (LBEL's sole shareholder) and the individual proposed to be appointed as a director of LBEL for the purposes of (among other things) declaring a dividend, to be canvassed and (as appropriate) put before the Court. The current status of the LBEL Administrators' application is that it has been adjourned pending a further hearing to be fixed.

LBH

- 14 LBH is an English limited company. LBH's principal activities were
 - 14.1 acting as the "pass through" vehicle for the transfer of subordinated debt and cash funding to LBIE;
 - 14.2 managing foreign currency accounts under a trust agreement for Lehman Brothers Asset Management (Europe) Limited; and
 - 14.3 playing an important role in the funding for UK Group companies.
- 15 LBH entered into administration on 15 September 2008. Its current administrators are Anthony Victor Lomas, Steven Anthony Pearson, Derek Anthony Howell, Julian Guy Parr and Gillian Eleanor Bruce (the "**LBH Administrators**"). On 2 May 2014, the High Court of Justice made an order granting permission for the LBH Administrators to make a distribution to creditors and on 13 June 2014 the LBH Administrators gave notice to creditors pursuant to Rule 2.95 of their intention to distribute. On 2 February 2016, the LBH Administrators declared a second interim dividend of 2 pence in the pound, which took the aggregate dividends paid to LBH's general unsecured creditors with proved claims to 6.08 pence in the pound in respect of such claims. The LBH Progress Report dated 9 February 2017 is at pages **39 to 55**.

- 16 LBH's key creditor – and therefore the party which will primarily benefit from further distributions from the LBH estate – is LBL.

Appendix 2: Summary of the Waterfall I Application

- 1 On 14 February 2013, in anticipation of a possible Surplus, the LBIE Administrators, together with the LBL Administrators and the LBHI2 Administrators, issued an application for directions (the “**Waterfall I Application**”) (a copy of which is at **pages 166 to 172**) as to (among other issues):
 - 1.1 the relative priority for payment, in the event of a Surplus, of:
 - (a) Statutory Interest and
 - (b) the Sub-Debt);
 - 1.2 whether or not Currency Conversion Claims exist, and where they rank for payment in the event of a Surplus;
 - 1.3 whether Statutory Interest accrued but unpaid in the LBIE Administration would be payable in a subsequent liquidation of LBIE;
 - 1.4 whether the respective obligations of LBL and LBHI2 under Section 74 extend not only to provable debts but also to Statutory Interest and Currency Conversion Claims; and
 - 1.5 whether LBIE can prove in the administrations or liquidations of its members in respect of their liabilities to contribute to any shortfall in LBIE’s assets under Section 74 while LBIE is in administration.
- 2 Following a hearing before Mr Justice David Richards in November 2013, on 14 March 2014 the Judge handed down his judgment on the Waterfall I Application (the “**Waterfall I Judgment**”).
- 3 In relation to the issues outlined above at paragraph 1, Mr Justice David Richards concluded (see paragraph 250 of the Waterfall I Judgment):
 - 3.1 that the Sub-Debt ranks for payment behind provable debts, Statutory Interest and Non-Provable Claims in the event of a Surplus;
 - 3.2 that Currency Conversion Claims exist as a non-provable liability and therefore rank for payment ahead of the Sub-Debt in the event of a Surplus;

- 3.3 that if LBIE moved from administration into liquidation without having paid Statutory Interest accrued in the LBIE Administration, Statutory Interest would only be payable to creditors from the date of liquidation. The interest in respect of the period of administration would not be provable by creditors in the subsequent liquidation nor would it be payable to creditors as Statutory Interest under Rule 2.88 or under Section 189, but creditors whose debts carried interest apart from the administration (whether by contract, judgment interest or otherwise) would have a non-provable claim against LBIE in liquidation for any such interest in respect of the period of administration;
 - 3.4 that the obligations of LBL and LBHI2 under Section 74 extend not only to provable debts but also to Statutory Interest and Currency Conversion Claims; and
 - 3.5 that whilst LBIE remains in administration, LBIE (acting by the LBIE Administrators) could prove on a contingent basis in the distributing administrations or subsequent liquidations of LBL and LBHI2 for their respective liabilities under Section 74 (the relevant contingencies including LBIE's entry into liquidation and a call being made under Section 74 by LBIE's liquidators).
- 4 Commencing on 23 March 2015, the Court of Appeal heard an appeal of all issues in the Waterfall I Application (the "**Waterfall I Appeal**"). On 14 May 2015, the Court of Appeal handed down its judgment (the "**Waterfall I Appeal Judgment**"). The Court of Appeal's directions in respect of the issues were as follows:
- 4.1 The Court of Appeal held (upholding the Waterfall I Judgment) that the Sub-Debt:
 - 4.1.1 is a provable debt in LBIE's insolvency and that it ranks for payment by LBIE after payment of all proved debts, Statutory Interest thereon and Non-Provable Claims; and
 - 4.1.2 is a contingent debt, with the relevant contingencies being payment in full of proved debts, Statutory Interest and Non-Provable Claims.
 - 4.2 The Court of Appeal by a majority (Moore-Bick and Briggs LJ) agreed with the Judge that Currency Conversion Claims exist as the balance of a creditor's original contractual claim which has not been discharged by the process of conversion, proof and dividend under the relevant part of the insolvency scheme, and rank as

non-provable liabilities of LBIE to be paid after all proved debts and Statutory Interest thereon. Lewison LJ dissented.

- 4.3 In relation to Statutory Interest accruing on proved debts during the period of LBIE's administration, the Court of Appeal departed from the Judge's reasoning and found that, once a Surplus has arisen in the LBIE Administration after payment of all proved debts, Rule 2.88(7) has the effect of requiring the surplus funds in the LBIE Administration to be used in discharging Statutory Interest on the debts proved in the LBIE Administration before being used for any other purpose such that it continues to burden so much of the Surplus arising in the LBIE Administration as passes into the hands of the liquidator.
- 4.4 The Court of Appeal agreed with the Judge that the liability of members under Section 74 extends not only to provable debts but also to Statutory Interest and liabilities not provable as part of the statutory scheme (such as Currency Conversion Claims).
- 4.5 The Court of Appeal agreed with the Judge that LBIE could (whilst in administration and acting through the LBIE Administrators) prove for the contingent Section 74 liabilities of its members in their distributing administrations or subsequent liquidations.
- 5 All of the issues determined in the Waterfall I Appeal Judgment were subject to appeals to the Supreme Court. The Supreme Court heard an appeal of all issues in the Waterfall I Application during a four-day hearing from 17 October 2016 to 20 October 2016.
- 6 On 17 May 2017, the Supreme Court handed down the SC Judgment.

Appendix 3: Summary of the Waterfall II Application

- 1 On 12 June 2014, the LBIE Administrators issued an application for directions in relation to further issues relating to the Surplus (the **"Waterfall II Application"**) (a copy of which is at **pages 173 to 189**). Those issues broadly fell, and were ultimately divided for the purposes of case management, into three categories:
 - 1.1 how entitlements to Statutory Interest and Currency Conversion Claims are to be calculated (**"Waterfall IIA"**), including whether Statutory Interest is to be calculated on the basis of allocating dividends:
 - 1.1.1 first to the payment of accrued Statutory Interest at the date of the relevant dividends and then in reduction of the principal; or
 - 1.1.2 first to reduction of the principal and then to the payment of accrued Statutory Interest;
 - 1.2 whether terms contained in certain post-administration contracts entered into between LBIE and creditors had the effect of releasing creditors' entitlements to Statutory Interest and Currency Conversion Claims and, if so, whether the LBIE Administrators should be directed not to enforce them (**"Waterfall IIB"**); and
 - 1.3 how default interest is to be calculated under ISDA Master Agreements and certain other trading agreements, including what forms of funding may be included when assessing a non-defaulting party's "cost of funding" for the purpose of calculating such default interest (**"Waterfall IIC"**).
- 2 The trials of the Waterfall IIA and Waterfall IIB issues took place before Mr Justice David Richards between 18 and 26 February 2015 and 18 and 21 May 2015 respectively. Mr Justice David Richards handed down his judgments (the **"Waterfall IIA Judgment"** and **"Waterfall IIB Judgment"**) on 31 July 2015 and orders (the **"Waterfall IIA Order"** and **"Waterfall IIB Order"**) on 27 November 2015. Copies of those documents have been included in RD11 as follows:
 - 2.1 the Waterfall IIA Judgment at **pages 190 to 248**;
 - 2.2 the Waterfall IIB Judgment at **pages 249 to 295**;
 - 2.3 the Waterfall IIA Order at **pages 296 to 303**; and

2.4 the Waterfall IIB Order at **pages 304 to 307**.

- 3 Further to the Waterfall IIA Judgment and Waterfall IIB Judgment, the parties identified certain further issues which are closely related to, and/or arise directly from, issues covered in those judgments. The Court agreed to give supplemental judgments in relation to supplemental issues 1(b), 1(c), 2-5 on 24 August 2016 (the "**Waterfall II Supplemental Issues Judgment**") and an order on 17 October 2016 (the "**Waterfall II Supplemental Issues Order**"). Copies of those documents have been included in RD11 as follows:

3.1 the Waterfall II Supplemental Issues Judgment at **pages 304 to 324**; and

3.2 the Waterfall II Supplemental Issues Order at **pages 325 to 328**.

- 4 The trial of Waterfall IIC (including Waterfall IIA and Waterfall IIB supplemental issue 1(a)) took place before Mr Justice Hildyard between 9 and 25 November 2015. Mr Justice Hildyard handed down the Waterfall IIC judgment (including Waterfall IIA and Waterfall IIB supplemental issue 1(a)) on 5 October 2016 (the "**Waterfall IIC Judgment**"). Following the Waterfall IIC Judgment, a consequential hearing regarding matters arising from the Waterfall IIC Judgment was listed for 12 December 2016 and Mr Justice Hildyard handed down his judgment on the Waterfall IIC consequential matters hearing on 16 December 2016 (the "**Waterfall IIC Consequential Matters Order**"). Copies of those documents have been included in RD11 as follows:

4.1 the Waterfall IIC Judgment at **pages 329 to 479**; and

4.2 the Waterfall IIC Consequential Matters Order at **pages 480 to 488**.

- 5 Commencing on 3 April 2017, the Court of Appeal heard an appeal of all supplemental issues (including supplemental issue 1(a)) together with appeals on the Waterfall IIA Judgment and the Waterfall IIB Judgment issues in the Waterfall I Application (the "**Waterfall IIA & B Appeal**"). The Court of Appeal has ordered further written submissions, and a further oral hearing on 25 July 2017, in relation to the impact of the SC Judgment on the Waterfall IIA & B Appeal.
- 6 The Court of Appeal will also hear an appeal on the Waterfall IIC Judgment, with the hearing listed to commence on 3 July 2018.

Appendix 4: Claims among LBIE and the Affiliates

- 1 This Appendix sets out the various claims the LBIE and the Affiliates have against one another and the current status of those claims
- 2 On 22 July 2014, LBHI2 submitted a proof of debt in the administration of LBL in the sum of £257m (which the LBIE Administrators understand to be in respect of the intercompany balance between LBHI2 and LBL as at 15 September 2008).
- 3 On 31 October 2014, LBIE submitted a claim for c.£10.4bn in LBL's administration, which comprises:
 - 3.1 a £10bn claim which is the LBIE Administrators' prudent assessment of LBL's contingent liability to LBIE as a contributory under Section 74;
 - 3.2 a £119 million claim in respect of a pension debt arising under Section 75 Pensions Act 1995 and assigned to LBIE by the trustees of the Lehman Brothers pensions scheme; and
 - 3.3 a £254 million claim arising from the general intercompany position between LBIE and LBL.
- 4 On 7 November 2014, LBIE asserted a £10bn claim against LBHI2 in respect of LBHI2's contingent liability to LBIE as a contributory under Section 74.
- 5 LBIE's contingent claim under Section 74 in the amount of £10bn as included in its proof against LBL, and its statement of claim delivered to LBHI2 was based on the LBIE Administrators' then prudent assessment of potential claims against the Surplus. Depending on the eventual amount of the Surplus and the outcomes of the various Waterfall applications there is a range of potential outcomes, including scenarios in which the Surplus might be insufficient to meet the remaining claims against LBIE such that LBIE would wish to make claims against its unlimited liability members, LBL and LBHI2, under Section 74. This claim was made prior to the SC Judgment, which impacted materially the extent of Contribution Claims that might be made.
- 6 LBL and LBHI2 have submitted proofs of debt in the LBIE Administration as follows:
 - 6.1 On 21 December 2011, LBL submitted a proof of debt for an unsecured claim of around £363m;

- 6.2 On 23 September 2015, LBL requested leave of the LBIE Administrators to amend its proof of debt to £10.934bn (the “**Amended LBL Proof**”) to claim a recharge of, amongst other things:
- 6.2.1 LBIE’s estimate of LBL’s contingent liability to LBIE as a contributory under Section 74 in the amount of £10bn;
 - 6.2.2 administration expenses incurred by LBL, in the amount of £30m;
 - 6.2.3 the unrecovered balance of claims made by LBL in the insolvent estates of other Lehman Brothers entities, where a dividend of less than 100p in the pound is expected, in the amount of £535m;
 - 6.2.4 sums payable in respect of a claim by Canary Wharf Group, the landlord of the Lehman Brothers group’s former European headquarters at 25 Bank Street, in the amount of £211.9m; and
 - 6.2.5 further purported recharges.
- 6.3 On 6 April 2016, the LBIE Administrators confirmed their consent (to the extent such consent was required) to LBL’s request to amend its proof;
- 6.4 On 24 April 2012, LBHI2 submitted a proof of debt for an unsecured claim of around £38m and for an unsecured subordinated claim in respect of sums advanced to LBIE under three subordinated debt agreements dated 1 November 2006 in the amount of around £1.254bn (the “**Sub-Debt**”).
- 7 On 23 September 2015, LBL submitted a proof of debt in LBHI2’s estate in the sum of £10bn, in respect of a recharge of LBIE’s estimate of LBL’s contingent liability to LBIE as a contributory under Section 74.
- 8 On 31 August 2012, LBL submitted a proof of debt in LBEL’s estate in the sum of £243m, in respect of the intercompany balance between LBL and LBEL as at 15 September 2008 and the recharge of certain matters not included in the intercompany balance.
- 9 On or around 31 January 2014, LBHI2 served a notice on LBIE and the LBIE Administrators pursuant to Rule 2.104, confirming that LBHI2 had assigned such right title and interest as it had in and to its claim in respect of:

- 9.1 the unsecured claim of around £38m to Wentworth Sons Senior Claims S.à.r.l. ("**Wentworth Senior**"); and
 - 9.2 the Sub-Debt to Wentworth Sons Sub-Debt S.à.r.l ("**Wentworth Sub-Debt**"). I shall refer to Wentworth Senior and Wentworth Sub-Debt together as "**Wentworth**".
- 10 On 23 September 2015, LBL requested leave of the LBEL Administrators to amend its proof of debt to £4.9bn to include the recharge of the claims referred to in the Amended LBL Proof, such claims being:
 - 10.1 the recharge of LBIE's asserted contingent claim pursuant to Section 74 (valued at £4.5bn);
 - 10.2 the recharge of administration expenses incurred by LBL (valued at £22m); and
 - 10.3 the recharge of the unrecovered balance of claims made by LBL in the insolvent estates of other Lehman Brothers entities, where a dividend of less than 100p in the pound is expected (valued at £399m).
- 11 On 12 November 2015, the LBEL Administrators consented to LBL's request to amend its proof.
- 12 On 9 September 2014 LBEL submitted a proof of debt in LBL's estate in the sum of £447m, in respect of aspects of the intercompany balance that it considered ought to be reversed.
- 13 Presently:
 - (a) none of LBHI2's, LBIE's or LBEL's proofs have been adjudicated upon by the LBL Administrators;
 - (b) neither LBL's nor LBHI2's proofs have been adjudicated upon by the LBIE Administrators;
 - (c) LBL's proof has not been adjudicated upon by the LBEL Administrators; and
 - (d) the LBHI2 Administrators have not adjudicated upon LBL's proof, nor determined LBIE's claim.

Appendix 5: Issues in the Waterfall III Application

- Issue 1:** Whether the obligations of [LBHI2] and/or [LBL] to contribute to the assets of [LBIE] pursuant to Section 74 include an obligation to contribute to the assets of LBIE to the extent necessary to enable LBIE to pay [the Sub-Debt].
- Issue 2:** Whether any claim of LBIE against LBHI2 and/or LBL under section 74 (a “**Contribution Claim**”) in respect of the Sub-Debt (a “**Sub-Debt Contribution Claim**”) is to be included in the insolvency set-off account in LBIE’s administration as against the provable claims of: (i) LBHI2; and/or (ii) LBL.
- Issue 3:** Whether the value of the Sub-Debt Contribution Claim, for the purposes of proof and set-off, is (i) for the full amount of the Sub-Debt; (ii) limited to the estimated value that is applied to LBHI2’s claim for the Sub-Debt for the purposes of proof; or (iii) some other value.
- Issue 4:** To the extent that insolvency set-off has already taken effect in the administration of LBIE between LBHI2’s claim in respect of the Sub-Debt and LBIE’s Sub-Debt Contribution Claim (if any) against LBHI2, what effect (if any) such set-off has on LBIE’s ability to make a Sub-Debt Contribution Claim again LBL.
- Issue 5:** In circumstances where insolvency set-off in LBIE’s administration took effect on 4 December 2009, whether insolvency set-off in a subsequent distributing administration or liquidation of LBHI2 and/or LBL is of any application in respect of those companies’ claims against, and liabilities to, LBIE.

Issue 6: In circumstances where insolvency set-off in the administration of [LBEL] took effect on 11 July 2012, whether insolvency set-off in a subsequent distributing administration or liquidation of LBL is of any application in respect of LBL's claims against, and liabilities to, LBEL.

Issue 7: In light of the fact that LBL owns one share of \$1 in LBIE and LBHI2 owns 2 million 5% redeemable Class A preference shares of \$1,000 each, 5.1 million 5% redeemable Class B shares of \$1,000 each and 6,237,133,999 ordinary shares of \$1 each in LBIE:

- i. whether their obligations to contribute to the assets of LBIE pursuant to Section 74 are joint and several, joint, several, or otherwise as against LBIE;
- ii. whether they are entitled to a contribution or indemnity from one another in respect of (a) any payments made pursuant to any such obligations; and/or (b) any set-off pursuant to any such obligation, and if so, the nature and extent of such right of contribution or indemnity;
- iii. whether, in addition to or instead of any right of contribution or indemnity... LBL or LBHI2 are liable to contribute to LBIE's assets to any amount sufficient for the adjustment of the rights of the contributories among themselves and what the effect of such adjustment is;
- iv. to what extent any right of contribution or indemnity... and/or adjustment... is affected by any other claims which LBHI2 and LBL have against one another or any other party;
- v. whether the [LBIE Administrators] should be directed to assert less than 100% of the Contribution Claim against LBL and/or LBHI2 and, if so, by how much the Contribution Claim should be reduced as against LBL and/or LBHI2 and what factors should the Court take into account in reaching this decision.

- Issue 8:** How, if at all, any claim for a contribution or indemnity... and/or any adjustment ... would be affected by the rule against double proof in circumstances where LBIE had not yet been paid in full in respect of a Contribution Claim.
- Issue 9A Preliminary Issue:** Whether, as a matter of law, it is possible for a member of a company to enter into with that company an enforceable agreement which has the effect of enabling that member to avoid what would be otherwise be its obligation to contribute to the assets of the company under Section 74 in the event of the company's winding up or otherwise to reverse the effect of that section (whether by claiming to be contractually entitled to reimbursement from that company in respect of such contributions or otherwise.
- Issue 9:** Whether and to what extent LBL is entitled, under the terms of the Service Agreement between LBL and LBIE dated 20 May 2004 or otherwise, to recover from LBIE:
- i. sums paid or payable by it to LBIE in respect of a Contribution Claim;
 - ii. sums claimed by LBL from insolvent members of the [UK] Lehman group of companies but not ultimately recovered from such companies ('Bad Debt Claims'); and
 - iii. certain (and if so, which) expenses of LBL's administration.
- Issue 10:** If the answer to the issue at sub-paragraph 9(i) above is yes, whether LBL's recharge claim against LBIE in respect of the Sub-Debt Contribution Claim and LBHI2's claim in respect of the Sub-Debt are to be paid *pari passu* and, if not, in what order or priority.
- Issue 11:** Whether and to what extent LBL is entitled, under the terms of the Service Agreement between LBL and [LBEL] dated 20 May 2004 or otherwise, to recover from LBEL:
- i. sums paid or payable by it to LBIE in respect of a Contribution Claim;

- ii. Bad Debt Claims claimed by LBL; and
- iii. certain (and if so, which) expenses of LBL's administration.

Issue 12: If the answer to the question set out at paragraph 11(i), 11(ii) or 11(iii) above would otherwise be in the affirmative, is it impacted (and if so, to what extent) by any set-off occurring in LBIE's administration as between (i) the Contribution Claim and (ii) provable claims of LBL against LBIE.

Issue 13: Whether the share register of LBIE ought to be rectified (a) on the basis that LBL did not hold a share in LBIE or (b) on any other basis, or LBL should, on any other basis, not have the liabilities of a member of LBIE, notwithstanding its holding of a LBIE share.

Issue 14: Whether and to what extent LBL is entitled to recover from LBH sums paid or payable by it to LBIE in respect of a Contribution Claim.