A3/2016/4213

IN THE COURT OF APPEAL

ON APPEAL FROM

No 7942 of 2008

IN THE HIGH COURT OF JUSTICE

CHANCERY DIVISION

COMPANIES COURT

[2016] EWHC 2131 (Ch)

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

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

WENTWORTH SONS SUB-DEBT S.À R.L (1) ANTHONY VICTOR LOMAS

Appellant

- and -

(1) STEVEN ANTHONY PEARSON

(2) PAUL DAVID COPLEY

(3) RUSSELL DOWNS

(4) JULIAN GUY PARR

(as the joint administrators of the above named company)

(5) BURLINGTON LOAN MANAGEMENT LIMITED

(6) CVI GVF (LUX) MASTER S.À R.L

(7) HUTCHINSON INVESTORS LLC

(8) YORK GLOBAL FINANCE BDH, LLC

Respondents

SKELETON ARGUMENT ON BEHALF OF WENTWORTH

ON SUPPLEMENTAL ISSUES ARISING IN WATERFALL PARTS IIA AND IIB

SUPPLEMENTAL ISSUE 3

Whether, and if so to what extent, a non-provable claim to interest on a Currency Conversion Claim should be reduced by interest received by the creditor pursuant to Rule 2.88 on its proved debt.

Wentworth's position

1. This issue arises only if Wentworth is unsuccessful in its appeal against the Judge's conclusion that a creditor with an interest bearing foreign currency debt has a non-provable claim to interest on any currency conversion claim that arises in respect of that debt (Declaration (vi) of the Order of 9/10/15 in Waterfall IIA). For the reasons set out in paragraphs 7-22 of its appeal skeleton dated 1/2/16, Wentworth contends that decision was wrong.

2. If, however, there is a non-provable claim to interest on a currency conversion claim, Wentworth contends for a limited form of offset between the non-provable claim for interest on the currency conversion claim and Statutory Interest received pursuant to Rule 2.88 as follows. The non-provable claim to interest should be reduced by Statutory Interest received by the creditor pursuant to Rule 2.88 on its proved debt, if and to the extent that the total interest that would be received by the creditor relating to the period after the Date of Administration[1] (including Statutory Interest and interest on its Currency Conversion Claim) exceeds the creditor's contractual right to interest on its foreign currency debt (i.e. exceeds, when converted into the relevant foreign currency at the date received, the interest which the creditor would have been entitled to receive for that same period on its foreign currency debt had that debt not been converted into sterling at the Date of Administration).

[1] Before the Judge, Wentworth argued for an offset relating to the period between the Date of Administration and the date of the final dividend payment. However, the logic of the argument extends to the whole period after the Date of Administration, such that no interest on the currency conversion claim should be allowed which would result in the creditor receiving *more* (when converted into the relevant foreign currency) than it was contractually entitled to, irrespective of the period to which payments of interest received by it related.

Submissions in support of Wentworth's position

3. The reasons set out in paras 7-22 of Wentworth's skeleton dated 1/2/16 are also pertinent to its appeal on Supplemental Issue (3). Two points are of particular importance:

(1) First, underlying Wentworth's appeal on both issues is the contention that a currency conversion claim is, properly understood, not a separate claim independent from the process of proof, but is merely such part of the creditor's underlying claim (i.e. the claim which is provable) which remains "unpaid" in the foreign currency following payment in full of sterling dividends; and

(2) Second, a currency conversion claim is payable only after Statutory Interest has been paid on all proved debts, for the period between the date of administration and the date of payment of the final dividend, pursuant to Rule 2.88.

4. Thus, interest on a currency conversion claim, is interest upon a *part* of the underlying debt which has been admitted to proof, upon the *whole* of which the creditor has already received Statutory Interest

5. The limited form of offset for which Wentworth contends is intended merely to reflect the fact that both Statutory Interest and interest on a currency conversion claim are referable to the same debt. The claim to interest on a currency conversion claim is based on a reversion to the creditor's contractual rights on which its proved debt is based. Accordingly, where a creditor has received Statutory Interest on its proved debt which when converted into the relevant foreign currency at the time of receipt is equal to its underlying contractual entitlement to interest in the foreign currency, it should not be entitled to receive any further payment of interest by reference to its (now fully satisfied) contractual rights.

6. The point is best illustrated by a simple example which assumes a creditor with a contractual right to interest at a lower rate than the Judgments Act rate:

(1) The creditor has a claim for $100 and a contractual claim to interest at 4% per annum.

(2) As at the Date of Administration £1 = $2, so the claim when converted into a sterling sum gives a proved debt of £50.

(3) Two years later, the proved debt (£50) is paid in full. At that point sterling has weakened against the dollar such that £1 = $1.50, and £50 is therefore worth $75.

(4) The creditor therefore has a Currency Conversion Claim of $25.

(5) The creditor is entitled to Statutory Interest at 8%, payable on the proved debt of £50, for two years, i.e. £8. Assuming no further change in exchange rate, the amount of Statutory Interest received by the creditor, once converted into dollars (at £1 = $1.50), is $12.

(6) Pursuant to its contract, the creditor, but for the administration, would have been entitled to interest at 4% on $100, relating to that two year period, namely $8.

(7) It has, therefore, already received more than the total amount of interest (in dollars) it was entitled to receive pursuant to its contract for the relevant period on its whole dollar claim.

(8) In this example, therefore, the claim for interest on the Currency Conversion Claim should be reduced to zero.

7. The requirement for an offset is not limited to cases where the creditor's contractual entitlement to interest is at a rate lower than the Judgments Act rate. It may also arise, even in the case of a creditor with a contractual right to interest equal to, or even greater than, the Judgments Act rate, if – as a result of a reversal in FX movements in the period between the date when the final dividend is paid and the date when Statutory Interest is paid – the creditor receives more interest, once converted into the foreign currency, than its contractual entitlement.

8. In rejecting Wentworth's submissions, the Judge held that Statutory Interest under Rule 2.88 is "*payable by law on the proved debt and is referable only to the proved debt*" (at [52] and [53]). He specifically rejected Wentworth's submission that the currency conversion claim represents that portion of the proved debt that is not satisfied by payment of dividends, holding that "*the proved debt is the sterling sum and it has been satisfied in full by the dividends*". Wentworth contends that the Judge here fell into error, because the proved debt is the single, indivisible, obligation owed to the creditor. The conversion of the debt into sterling for the purpose of proof does not create a new, separate, obligation. Any payment, whether by way of dividend or Statutory Interest, is referable to that single, indivisible, obligation.

9. If the offset for which Wentworth contends is not permitted, then foreign currency creditors stand to benefit from an overpayment to the disadvantage of other non-provable and lower-ranking claims.

SUPPLEMENTAL ISSUE 5

Whether, to the extent that a creditor has a non-provable claim for interest on a Currency Conversion Claim, such non-provable claim has been released under the terms of the CRA and/or CDD and if so, whether the Administrators would be directed not to enforce such release(s).

10. The Judge held (in Waterfall IIB) that on their true construction neither the CRA nor the CDDs released a creditor's currency conversion claim and, if that was wrong, the administrators would nevertheless be directed to pay currency conversion claims pursuant to the principle in *ex parte James* and/or under paragraph 74 of Schedule B1 to the Insolvency Act 1986.

11. The Judge further held, in the judgment on supplemental issues, that:

    (1) To the extent that a creditor had a non-provable claim to interest, it was released by the terms of the CRA and the CDDs;

(2) The administrators would not be directed to pay such interest, whether by application of the principle in *ex parte James* or under paragraph 74 of Schedule B1;

(3) The CRA released a creditor's non-provable claim to interest on a currency conversion claim; but that

(4) The CDDs did not release a creditor's non-provable claim to interest on a currency conversion claim and, if that was wrong, the administrators would be directed to pay such interest pursuant to the principle in *ex parte James* and/or under paragraph 74 of Schedule B1.

12. In its main appeal skeleton on Waterfall IIB Wentworth contends that a creditor who entered into a CDD where the Agreed Claim Amount was expressed in Sterling has released any currency conversion claim. If it is successful in that appeal, it must follow that any claim to interest on such currency conversion claim has also been released.

13. If and to the extent that a currency conversion claim has not been released by the terms of any CDD, however, Wentworth contends that the terms of each CDD have nevertheless released a claim to interest on any currency conversion claim.

14. As noted above, the Judge concluded that the terms of the CRA released any claim to interest on a currency conversion claim. He did so in reliance on clauses 20.4.7 and 25.1 of the CRA (see paragraphs 64 and 65 of the judgment on supplemental issues dated 24/8/16). The reasoning, in summary, is as follows:

(1) Clause 25.1 of the CRA states: "*for the avoidance of doubt, no interest shall accrue on any Net Financial Claim, save to the extent provided in Rule 2.88 of the Insolvency Rules.*"

(2) A "*Net Financial Claim*" is defined as any positive Net Contractual Position. The Net Contractual Position is either (in the case of only one Financial Contract between LBIE and the creditor) the close-out amount under that contract or (in

the case of more than one Financial Contract between LBIE and the creditor) the aggregate of the close-out amounts under each such contract. (See clause 24.2 of the CRA, and [112] of the *Waterfall IIB* judgment [2015] EWHC 2270 (Ch).)

(3) By clause 24.1 of the CRA, all close-out amounts shall be denominated in US dollars. Any Net Financial Claim would therefore similarly be denominated in US dollars.

(4) The prohibition on interest accruing on any Net Financial Claim, save to the extent provided in Rule 2.88, clearly precludes any non-provable claim for interest in respect of the US dollar denominated contractual claim. Accordingly, there is no subsisting contractual right to interest (on the dollar denominated contractual claim) to which the creditor could be remitted, following the entry by it into the CRA.

15. Wentworth contends that the same reasoning, and conclusion, applies to the CDDs.

16. By clause 2.3 of the Admitted Claim CDD the mutual release of all claims between LBIE and the creditor expressly includes "*all Claims for interest … whether arising under the Creditor Agreement or not*". At the very least, therefore, this expressly releases any claim for interest arising under the Creditor Agreement. The Creditor Agreement is defined in each CDD as the underlying financial contract (e.g. ISDA or other Master Agreement) pursuant to which the creditor's claim arises.

17. The possibility of a currency conversion claim arises where the creditor's claim is, by virtue of its Creditor Agreement, denominated in a foreign currency. The currency conversion claim is the unpaid portion of its claim under the Creditor Agreement. In order for a creditor to be entitled to interest on a Currency Conversion Claim, it must have an entitlement to interest in the Creditor Agreement, and the non-provable claim to interest on a currency conversion claim is based on the remission to that contractual right: see *Waterfall IIA* judgment [2015] EWHC 2269 (Ch) at [169].

18. The express release in the CDDs of interest arising under the Creditor Agreement thus removes the essential ingredient of a claim to interest on currency conversion claims, namely a continuing entitlement to interest on any amounts due under the Creditor Agreement. There is no reason not to give effect to the clear, express wording in the CDDs.[2]

19. Accordingly, the Judge should have held – consistently with his conclusion in relation to the CRA, and consistently with his conclusion in relation to non-provable claims to interest generally, that the CDD had the effect of releasing any non-provable claim to interest on a currency conversion claim.

20. The Judge, at paragraph 67 of the judgment on supplemental issues dated 24/8/16, concluded that if – as he had held – the CDDs did not release a currency conversion claim, then it follows that "*it is not a plausible construction to read the general words "including all Claims for interest" as extending to contractual interest on currency conversion claims*." Wentworth contends that the Judge erred, in this passage, in that:

    (1) He failed to take account of the fact that a claim to interest on a currency conversion claim is a claim to interest on a portion of the claim arising under the Creditor Agreement;

    (2) He thus failed to take account of the fact that the clear intention of the express words in clause 2.3 of the Admitted Claims CDD (releasing all claims to interest arising under the Creditor Agreement) was to exclude *any* claim to interest (save for interest under Rule 2.88) arising under the Creditor Agreement; and

    (3) There is no basis for discriminating (so far as the release of interest claims is concerned) between interest arising under a Creditor Agreement where the

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[2] In the insolvency of the Lehman entities in the US, when a similar question arose as to the effect of a settlement agreement (which resulted in an Allowed Claim for the purposes of the Chapter 11 Plan of distribution) on a prior contractual right to interest, it is noteworthy that the court relied on the principle that "t*he best evidence of what parties to a written agreement intend is what they say*" in concluding that the settlement agreement precluded reliance on the terms of the prior contract: see re Lehman Brothers Holding Inc, 12 January 2017, United States Bankruptcy Court, Southern District of New York Case No.08-13555 (SCC).

claim is denominated in sterling, and one where it is denominated in a foreign currency.

21. If the Court accepts the above submission, it is then necessary to consider whether the Judge was correct to hold that, in any event, he would have restrained the enforcement by the Administrators of the releases in the CDDs pursuant to the rule in *ex parte James* or paragraph 74 of Schedule B1.

22. In so holding the Judge was wrong in law. First, the release of non-provable claims to interest is not an unintended effect of the CDDs:

    (1) the release of any and all claims to interest is an expressly stated effect of each CDD (clause 2.3 of the Admitted Claims CDD; clause 2.1.1 of the Agreed Claims CDD);

    (2) although an express carve-out was included for Statutory Interest in later CDDs, that had no effect on the release of any claim for interest *other* than that payable pursuant to Rule 2.88; on the contrary, it clarified and reinforced the release of any claim to interest apart from that payable pursuant to Rule 2.88;

23. Second, the effect of the proposed resolution of creditors' claims on claims to interest had been made clear from the outset of the Administrators' efforts to reach a resolution in respect of creditors' claims. In the draft explanatory statement for the proposed scheme, which had been prepared in conjunction with representatives of the creditors, it was clearly stated that "*no interest will accrue on any unpaid liability of LBIE from the Administration Date, save to the extent that such interest would accrue under Rule 2.88 of the Insolvency Rules*."[3] The circular for the CRA similarly noted that trust creditors would not be entitled to any interest on their claims against the company, including with respect to close-out amounts under open financial contracts.[4] The statement within each of the CDDs that any claim to interest would be released was clear in itself and needed no further explanation.

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3 See paragraph 9.8.7 of the draft Explanatory Statement.

4 See paragraph 4.7 of Reader's Guide to the CRA.

24. Third, there is no discrimination involved in enforcing the release of non-provable claims to interest, as any version of a CDD will have released such claims. Moreover (as noted above) the introduction of language into the later CDDs preserving claims to Statutory Interest creates no discrimination similar to that which the Court found was caused by the introduction of language into the later CDDs preserving Currency Conversion Claims. That is because the language preserving claims to Statutory Interest merely confirms and reinforces the release of any other claim to interest that had been a part of the CDDs all along.

25. If and to the extent that it is suggested that there is discrimination between (1) all those creditors who entered into either or both of the CRA and a CDD, and (2) all those creditors that entered into no bi-lateral agreement at all, then such suggestion should be rejected. While it is true that there would be different treatment as between those two groups of creditors, that is solely the product of the fact that the first group chose to take the material advantages of certainty, speedier resolution and distribution, and release of any other possible claims against them by LBIE, offered by entering into the CRA and/or a CDD and, as part of the price of those advantages, agreed to the wide-ranging release, including of any claims to interest, that was an express and integral part of the CRA and each CDD.

26. Accordingly, Wentworth contends that the Judge was wrong to hold that he would have directed the Administrators not to enforce any release of non-provable claims to interest in the CDDs, whether on the basis of *ex parte James* or paragraph 74 of Schedule B1.

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