Waterfall II application

IN THE HIGH COURT OF JUSTICE **No. 7942 of 2008**

CHANCERY DIVISION

COMPANIES COURT

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

AND IN THE MATTER OF THE INSOLVENCY ACT 1986

JOINT ADMINISTRATORS' POSITION PAPER

Introduction

1. This paper summarises the position of the joint administrators of Lehman Brothers International (Europe) (in administration) ("**LBIE**") (the "**Administrators**") in relation to the 39 issues arising for determination in the Waterfall II application. Capitalised terms used but not otherwise defined in this document are defined in the Waterfall II Application dated 12 June 2014 (the "**Application**").

2. The approach taken by the Administrators in this position paper reflects what the Administrators consider will be of greatest assistance to the Court in light of the three position papers that have been served by the Respondents (who will be referred to, following the definitions used in those position papers, as the "**Senior Creditor Group**", "**Wentworth**" and "**York**"), and the Administrators' knowledge and experience of this administration and of insolvency proceedings generally.

3. In particular, the Administrators are conscious that the Respondents (while broadly representative of certain, generally opposing, interests): (a) have not been, and will not be, formally appointed as representative respondents; and (b) might adopt positions which reflect their own (in some cases complicated) commercial interests rather than the positions that representative respondents would feel compelled to take. Indeed the Respondents have not, contrary to what might have been anticipated, taken all the (sensible) available positions in relation to certain issues. As a result the Administrators consider that, in respect of certain of the issues raised, not all of the possible positions and arguments have been adopted and ventilated in the Respondents' position papers (and are conscious that the Respondents' own commercial interests may lead to the positions currently advanced by the Respondents changing between now and trial).

4. Accordingly, the Administrators' approach, as reflected in this position paper, is as follows:

   4.1 Where all the Respondents have taken the same position and the Administrators do not consider that there is an arguable position to the contrary, the Administrators do not seek to advance a contrary position and will invite the Court to give directions in accordance with what has become an agreed position. The Administrators intend to give notice of their intention to do so on the LBIE administration website to give any creditor which disagrees with that approach the opportunity to make an application to intervene if it wishes.

   4.2 Where the Respondents have adopted a common position but the Administrators consider that there is a respectable argument which supports the contrary position, the Administrators set out the arguments in favour of that contrary position (whether or not the Administrators consider the position they are contending for to be the correct one), so as to ensure that the Court has the benefit of the competing arguments in determining the relevant issues.

4.3 In relation to issues where, on the face of the Respondents' position papers, the Administrators consider that all (sensible) available positions have been set out, the Administrators adopt positions on those issues on which, as experienced insolvency practitioners, the Administrators consider that they should adopt a positive position, being matters of insolvency law and/or matters relating to their knowledge and experience as Administrators of LBIE.

4.4 Where the Administrators adopt a position in respect of an issue which accords with that of one of the Respondents, but consider that that Respondent has not identified with sufficient clarity or particularity the arguments on which it will seek to support the position adopted, the Administrators set out those arguments that they consider the Court ought to have made to it, in order to ensure that the issue is fully argued, and (where appropriate) invite the relevant Respondent(s) in their reply position paper(s) more fully to articulate the position to ensure that the Court has before it all relevant arguments.

4.5 The Administrators are mindful that, in some circumstances, the interests of those ordinary unsecured creditors who are not represented in this Application might not be reflected in the position taken by any of the Respondents (for example where the claims to high rates of Statutory Interest advanced by one or more of the Respondents in the Application would have the effect of reducing the amount of assets available for payment of the interest entitlements of other creditors which are not advancing such claims). In such circumstances, the Administrators seek to ensure that arguments that would protect the interests of such creditors are fully ventilated and, where they consider appropriate in that context, express their position.

4.6 More generally, in relevant cases, the Administrators seek to provide the Court with further detail or context (including practical matters that arise with respect to those issues) with a view to identifying for the Court the

nature of the directions required to give the Administrators practical assistance in distributing the Surplus. The Administrators will (where appropriate) additionally file evidence in this regard.

4.7 In relation to certain issues, the Administrators consider that there are variations to the question posed, further propositions which require consideration, or ways in which certain issues overlap or interact with each other, which they have sought to identify. The Administrators invite the Respondents in their reply position papers to explain what position they take on those variations, propositions or further issues where their existing position papers do not make their positions clear.

5. Further and in any event, the Administrators reserve the right to amend, supplement or depart from any position (including a position of neutrality) or argument adopted below as they consider appropriate to ensure that all issues are fully and properly argued and to seek to ensure, so far as is possible, that the directions obtained from the Court on this Application will assist them to distribute the Surplus as quickly and efficiently as possible.

Statutory Interest

Construction of Rule 2.88

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

6. The Senior Creditor Group, Wentworth and York all take the same position on this issue, namely that the applicable rate of interest is simple rather than compound. This is an issue in respect of which the Administrators do not consider that there is an arguable position other than that on which the Respondents all agree.

7. Accordingly, the Administrators do not seek to advance a contrary position and intend to invite the Court to give directions in accordance with what has become an agreed position. The Administrators intend to give notice of their intention to do so on the LBIE administration website to give any creditor which disagrees with that approach the opportunity to make an application to intervene if it wishes.

8. On the basis that the correct position in relation to this issue is that the applicable rate of interest is simple rather than compound, the Administrators would propose that, for the purposes of determining creditors' entitlements in respect of Statutory Interest, the rate of 8% per annum be converted into a daily rate by dividing it by however many days there happen to be in a given calendar year. The Administrators invite the Respondents, in the event that they consider that this approach should not be adopted, to explain their reasons and the alternative approach they consider to be correct.

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

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

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

   (iii) on the basis of some other sequencing.

9. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions in relation to this issue. However, this is an issue on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law.

10. Accordingly, the Administrators' position in relation to this issue is that payments of dividends (i.e. dividends on proved debts) are to be allocated solely to the reduction of the proved debts. The Administrators note Wentworth's arguments in support of this position. However, the Administrators argue the position in their own way.

11. Rule 2.88 governs the accrual of interest on proved debts after the commencement of administration. Accordingly, this issue is purely a matter of statutory interpretation.

12. In this regard, Rule 2.88(7) makes it plain that payment of Statutory Interest may only occur after proved debts have been satisfied in full: "*Any surplus remaining after payment of the debts proved shall, before being applied for any purpose, be applied in paying interest on those debts in respect of the periods during which they have been outstanding since the relevant date* [the date, for present purposes, on which the company entered administration[1]]".

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[1] Pursuant to Rule 2.88(1).

13. The reference to "[a]*ny surplus remaining after payment of the debts proved*" (emphasis added) strongly suggests that: (i) payment of dividends to creditors to the point where it is identified that there is a surplus must have been as "payment of the debts proved" (i.e. the principal of the debts, not interest on them): (ii) no dividend may be allocated to the payment of Statutory Interest until all debts proved have been satisfied in full; and (iii) such payments from the surplus are in respect of interest (and not principal):

13.1. The phrase "*those debts*" used later in Rule 2.88(7) ("...*applied in paying interest on those debts*...") refers back to the earlier phrase "*the debts proved*".

13.2. The phrase "*the debts proved*" refers to those debts which are provable (for the purposes of Rule 12.3(1)) and have been proved. Those debts are, in effect, the principal of the creditors' debts, and specifically exclude interest.

13.3. The payment of Statutory Interest on "*those debts*" (i.e. "*the debts proved*") may only occur where there is a "*surplus*" in the relevant sense, and such payment must be made out of this "*surplus*".

13.4. A "*surplus*" in the relevant sense only arises once "*the debts proved*" have been paid, i.e. "*after payment of the debts proved*". Without more, the word "*payment*" must refer to the payment in full of all debts proved.

13.5. If the phrase "*the payment of the debts proved*" had been intended to mean something other than this, then one would expect it to be made clear by express words.

14. Accordingly, if Statutory Interest is payable only after proved debts have been satisfied in full, it cannot be that dividends are allocated first to the payment of Statutory Interest and then to the reduction of principal; indeed, the contrary is the case.

15. Further and in any event, the decision in *Bower v Marris* (1841) Cr. & Ph. 352 can have no relevance to interpreting Rule 2.88:

15.1 The ratio in *Bower v Marris* (a decision concerning a proved debt based on an interest bearing bond) was that payments to a creditor by way of dividend on a proved debt in bankruptcy should have no different effect from payments made by a solvent obligor[2].

15.2 In *Bower v Marris* the Lord Chancellor distinguished various decisions where dividends had been considered as an "*aliquot part of the debt upon which it is paid*"[3], on the basis that in those cases "*to adopt any other rule would work injustice, and defeat the contract between the parties*" (p.359).

15.3 Therefore, as regards the order in which dividends are allocated to principal and to interest, the effect of the rule in *Bower v Marris* was to remit the creditor to its contractual rights (whatever they may have been) in the event of a surplus.

15.4 The fact that the rule in *Bower v Marris* is incapable of applying where there is no "*rate applicable to the debt apart from the administration*" for the purposes of Rule 2.88(9) shows that the new law, after the 1986 legislative reforms, has moved away from the old law under *Bower v Marris*.

15.5 Further and in any event, the rule in *Bower v Marris* is inconsistent with the wording of Rule 2.88 and cannot have been intended to survive the coming into force of the 1986 legislation, even if it had previously had a wider application.

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2 "*Why should such payments have a different effect than they would have if made by a solvent obligor*?": p.357.

3 I.e. *Paley v. Field* (12 Ves. 435), *Bardwell v Lydall* (7 Bing. 489), *Raikes v Todd* (8 Ad. & Ellis, 846), and *Ex parte Holmes* (18 Law Journ. 33).

16. Further, and contrary to the Senior Creditor Groups' argument at paragraph 2(4) of their position paper, it follows from the fact that the present issue is purely a matter of statutory interpretation that:

16.1 It is nothing to the point that the so-called "*Bower v Marris* calculation" may be applied in other common law jurisdictions; and

16.2 It is also nothing to the point that, prior to the enactment of section 189 of the Act and Rule 4.93 of the Rules (and later Rule 2.88 in the context of administrations), the Court used to apply the so-called "*Bower v Marris* calculation" (as for example in *Re Lines Bros Ltd (No.2)* [1984] 1 Ch 438).

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

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

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

17. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions in relation to this issue. However, this is an issue on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law.

18. Accordingly, the Administrators' position in relation to this issue is that (ii) is correct.

19. The Administrators note the Senior Creditor Group's briefly stated arguments in support of (ii), but seek to argue this position in their own way.

20. The Cork Report, at paragraph 1385, advocated the payment of Statutory Interest and cited with apparent approval the conclusion of the Vice Chancellor

in the case of *Re Rolls Royce Ltd* [1974] 1 WLR 1584 that "*it seems fair that a creditor should be compensated for being kept out of his money during the period of administration if there turns out to be a surplus*".

21. The overarching purpose of the Statutory Interest provisions is to compensate creditors for being kept out of their money and deprived of their contractual (or other) rights as a result of the administration and the phrase "*rate applicable to the debt apart from the administration*" is intended to encompass a contractual rate (*Re Lehman Brothers International (Europe) (In Administration)* [2014] EWHC 704 (Ch), at paragraph 112).

22. There is no policy justification for seeking to deprive parties of their full contractual or other rights to interest once proved debts have been paid in full.

23. As such, the rate "*applicable to the debt apart from administration*" refers to the totality of the right to interest, taking into account both the percentage rate at which it is payable and the basis upon which it is payable (including whether it accrues on a simple or compound basis). This preserves the underlying rights of the creditors.

24. Moreover and in any event it is clear that, as a matter of language, the concept of a "*rate*" of something is well capable of meaning the amount of that thing determined in accordance with some rule or on some basis, without necessarily being limited to a mere percentage. More particularly, in the context of interest it is an equally sensible use of language to describe (for example) "9% simple interest" and "9% compounded with quarterly rests" as "rates" in the relevant sense.

25. Rule 2.88(9) provides a fall-back interest rate payable by an administrator, i.e. a "floor" of the Judgments Act Rate, but the creditor is entitled to claim a higher rate if he would be so entitled to it but for the administration.

26. The Court approved, in the context of non-provable interest in the Waterfall Application (*Re Lehman Brothers International (Europe) (In Administration)*

[2014] EWHC 704 (Ch), at paras 91 and 127), the statement of Giffard LJ in *In re Humber Ironworks and Shipbuilding Co,* L.R. 4 Ch. App. that: "*[a]s soon as it is ascertained that there is a surplus, the creditor whose debt carries interest is remitted to his rights under his contract*". Rule 2.88(9) achieves the same result in the context of Statutory Interest.

27. Furthermore, the Cork Report, in the context of considering amendments to the insolvency regime as regards interest, makes specific reference to the fact that, under the previous legislative framework, once there is a surplus after the proving creditors have been paid in full, the company is treated as being no longer insolvent with the result that: "*the creditor who is entitled to interest on the debt for which he has proved may recover the interest accruing after the presentation of the winding up petition as if there had been no winding up at all*" (paragraph 1384).

28. The notion of compensating a creditor for being kept out of his money by reference to a compounding interest rate calculation is commercially unobjectionable where that is what was agreed. In *Sempra Metals Ltd v IRC* ([2007] UKHL 34, 52), Lord Nicholls stated that:

> *"We live in a world where interest payments for the use of money are calculated on a compound basis. Money is not available commercially on simple interest terms... If the law is to achieve a fair and just outcome when assessing financial loss it must recognise and give effect to this reality."*

29. As a matter of construction, the term "rate" therefore includes not only the numerical rate but also the basis upon which that numerical rate is applied[4].

30. In light of the above, Wentworth's reliance at paragraph 24 of its position paper on the decision of the Federal Court of Australia in *Consolidated Fertilizers Ltd v Deputy Commissioners of Taxation* (1992) 107 ALR 456 is misplaced. That Australian decision concerned a statutory provision which provided for interest to be paid on a debt but was silent as to whether the applicable rate of interest

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4 Cf. *SMP Trustees Ltd v Keydata International Fund SPC* [2013] EWHC 3678 (Ch).

should be simple or compound. By contrast, the wording of Rule 2.88(9), in remitting the creditor to what its rights to interest would have been but for the debtor's entry into administration, provides the mechanism for determining in any given case whether the applicable rate should be simple or compound.

31. On the basis that the correct position in relation to this issue is that the words "*the rate applicable to the debt apart from the administration*" used in Rule 2.88(9) can refer to a compounding rate of interest, and provided that the answer in respect of Issue 2 is that Statutory Interest is calculated on the basis of allocating dividends first to the reduction of principal, the Administrators have identified a sub-issue, the Court's determination of which would assist the Administrators to distribute the surplus as quickly and efficiently as possible. This sub-issue is, where a creditor has a contractual or other entitlement to receive compound interest:

    31.1 whether accrued Statutory Interest continues to compound following the payment in full of the principal amount[5]; and

    31.2 if not, whether the creditor has a non-provable claim in respect of interest that would have continued to compound on a contractual basis following the payment in full of the principal amount.

32. In respect of the additional sub-issue identified in the previous paragraph, the Administrators invite the Respondents in their reply position papers to explain what position (if any) they take.

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

33. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions in relation to this issue. However, this is an issue

[5] See paragraph 163 below, in relation to issue 39, which may overlap with this issue.

on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law. In any event none of the Respondents has answered the question as to the circumstances in which a foreign judgment rate may apply (on which the Administrators require guidance in the event that the Court considers that the relevant words are apt to include such interest rate(s)). The Administrators invite the Respondents to set out their respective positions (on the assumption that such a rate is capable of applying).

34. The position the Administrators take is that the phrase "*the rate applicable to the debt apart from the administration*" in Rule 2.88(9) is capable of including a foreign judgment rate of interest or other Statutory Interest rate.

34.1 Rule 2.88(9) states that "*the rate of interest payable... is whichever is the greater of [8%] and the rate applicable to the debt apart from the administration*" (emphasis added).

34.2 The rate applicable to the debt apart from the administration means the rate applicable pursuant to the creditor's contractual or other right to interest which, but for the administration, the creditor would be entitled to seek judgment for or enforce.

34.3 Foreign law may provide for interest to accrue on amounts due pursuant to a judgment of the court, at a specified rate.

34.4 For example, French law provides for interest on such amounts at a rate of 4%, increasing to 9% two months after non-payment; German law provides for interest on such amounts at a rate equal to the aggregate of 8% and the basic rate as published by the Deutsche Bundesbank (currently -0.39%).

34.5 The rate applicable is "debt-specific" and the question is what the creditor's entitlement would have been, but for LBIE's entry into administration. The mere fact that a contract is governed by a foreign

law would not of itself be sufficient to entitle the counterparty to the foreign judgment rate. Such an entitlement would only arise where: (i) the creditor obtained a regular judgment which entitles it to the foreign judgment rate; (ii) the agreement specifically imports the judgment rate of a foreign jurisdiction as a contractual term (and that rate is more than 8%); or (iii) but for the administration, the creditor would have been able to sue in that foreign jurisdiction and enjoy the foreign judgment rate[6].

34.6 Wentworth contends at paragraph 29 of its position paper that the interpretation of Rule 2.88(9) favoured by the Administrators is wrong because it is premised upon an impossible counterfactual, i.e. "*upon action which a creditor could only take either in breach of the stay on commencing or continuing enforcement proceedings of its own*". This contention is misconceived since the fundamental object of Statutory Interest is to confer on a creditor, in the event of a surplus, a right to interest which the insolvency regime has prevented it from establishing either by proving or by commencing its own proceedings. See *Re Lehman Brothers International (Europe)* [2014] EWHC 704 (Ch), [2014] BCC 193, at [163]:

> "*The justification for statutory interest, even in those cases where the debts do not already carry a right to interest, is that the creditors are prevented by the liquidation regime from obtaining judgment against the company which would then carry interest at judgment rate.*"

35. Neither the Senior Creditor Group nor York, who adopt (like the Administrators) the position that the relevant words are apt to include a foreign

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6 If the Administrators are correct in relation to (ii), then two further issues arise on which the Administrators shall require guidance, and on which the Respondents are requested to set out their position in their reply position papers, specifically:

(a) In what circumstances will a creditor's ability to sue in a foreign jurisdiction (without actually doing so) give rise to a claim to interest based on a foreign judgment rate in the relevant sense; and

(b) From what date will interest based on such a foreign judgment rate begin to accrue, in circumstances where a creditor could have sued in the foreign jurisdiction as at the Date of Administration but has not done so?

judgment rate of interest, offers any indication as to the sorts of circumstances in which the present issue arises or is likely to arise. Accordingly, so as to give the Court a sense of the context in which the present issue arises, the Administrators intend to set out in evidence material as to where a foreign judgment rate of interest may be said to satisfy the Rule 2.88(9) definition of a "rate applicable to the debt apart from the administration".

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

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

   (ii) only the numerical rates themselves,

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

36. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions in relation to this issue. However, this is an issue on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law.

37. Accordingly, the Administrators' position in relation to this issue is that (i) is correct.

38. The Administrators note the Senior Creditor Group's briefly stated arguments in support of (i), but seek to argue this position in their own way:

    38.1 The rate "*applicable to the debt apart from administration*" refers to the totality of the right to interest, taking into account both the percentage rate at which it is payable and the basis upon which it is payable (i.e. on a simple or compound basis). This preserves the underlying rights of the creditors.

38.2 The purpose of Rule 2.88(9) is to give the creditor who is entitled to interest greater than 8% simple interest the benefit of having that greater right. A creditor who is entitled to interest payable at 7.99% compounded daily is entitled to receive that rate and is not limited to 8% simple interest simply because, as a strictly numerical matter, 8% is greater than 7.99%.

38.3 The percentage payable is only part of the creditor's entitlement and only part of the "rate". Rule 2.88(9) does not require one to take an uncommercial approach and to distinguish between the percentage payable and the application of that percentage.

38.4 Where the "*rate applicable to the debt apart from the administration*" varies from time to time, the administrator will have to calculate, on an aggregate basis, what interest the creditor would have been entitled to but for the administration and pay statutory interest based on that sum to the creditor if it is greater than the amount of interest which would be payable to the creditor on the basis of 8% simple interest.

38.5 Alternatively, the administrator is required to pay interest at the Judgments Act Rate for that part, or those parts, of the period during which the creditor's entitlement but for the administration was not greater than that rate and the greater rate for that part or those parts of the administration where the rate applicable but for the administration was greater than the Judgments Act Rate.

39. The Administrators strongly prefer their primary position that the calculation is based on the aggregate total of interest that the creditor would have received over the entirety of the relevant period, rather than on the various amounts of interest accruing in respect of discrete segments of the relevant period. The Administrators consider that the latter mode of calculation would give rise to considerable practical difficulties (if not impossibility) in establishing the greater rate for the purposes of Rule 2.88(9). In particular, this mode of calculation would be made difficult if interest rates were volatile during the

relevant period and/or if a compound contractual rate was required to be compared with the simple Judgments Act Rate.

40. There is also a further related issue to be resolved in relation to a proved debt only part of which arises from a contract (or contracts) conferring a right to interest (or which gives rise to a rate of interest in excess of the Judgments Act Rate). The issue is whether, in these circumstances, for the purposes of establishing "*whichever is the greater of the rate specified under paragraph (6) and the rate applicable to the debt apart from the administration*" under Rule 2.88(9), (a) one should compare the amount of Judgments Act Rate interest with the amount of contractual interest in respect of each constituent element of the proved debt or (b) one should not disaggregate the proved debt before making the comparison, such that the correct comparison is between the total amount of Judgments Act Rate interest which would accrue on the whole of the proved debt with the total amount of contractual interest which would accrue on the whole of the proved debt "*apart from the administration*". The Administrators invite the Respondents in their reply position papers to explain what position they take on this issue.

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

   (i) the Date of Administration;

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

   (iii) another date.

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

   (i) the Date of Administration;

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

having regard to whether:

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

a) the final dividend; or

b) Statutory Interest; and/or

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

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

(i) the Date of Administration;

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

(iii) another date,

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

(i) the final dividend; or

(ii) Statutory Interest

41. The Administrators consider that it would be helpful to deal with issues 6, 7 and 8 together, since they overlap in terms of the analysis involved in answering them. Further, while the question raised at issue 6 appears before those in issues 7 and 8 in the Application, in the Administrators' view it logically falls to be answered after those issues, since it only (or at least most obviously) in practice arises if the Court directs that the answer to issues 7 and/or 8 is (i) (i.e. the Date of Administration).

Issue 7

42. Dealing, therefore, first with issue 7, the Administrators consider the Respondents have, between them, taken all (sensible) available positions in relation to this issue. However, as experienced insolvency practitioners, the Administrators consider it appropriate to take a positive position on this issue, being a matter of insolvency law.

43. Accordingly, the Administrators' position in relation to this issue is that (ii) is correct.

44. The Administrators note Wentworth's arguments, as set out in its position paper, in support of this position. However, the Administrators would argue in favour of position (ii) in their own way:

    44.1 Contingent debts, although provable from the date of administration, become "outstanding" for the purposes of Rule 2.88(7) only when the debt becomes an actual debt.

    44.2 Accordingly, a creditor is not entitled to be paid Statutory Interest on a contingent debt which remains contingent as at the time dividends are paid. Statutory Interest is payable on contingent debts from the date on which the contingent debt ceases to be a contingent debt (including in circumstances where the contract was "closed out" after LBIE entered administration).

    44.3 Until a debt becomes an actual debt, it is not "outstanding" in the sense of being due and payable. It is in that sense that the word "outstanding" is used by the draftsman in Rule 2.88(7). This reflects the fact that, until a debt is due and payable, the administration does not operate so as to keep the creditor out of its money.

    44.4 Further, if Statutory Interest were payable from the date of administration, certain contingent creditors would receive a windfall. In particular, where a creditor's contingent claim has not crystallised until some time after the date of administration then the creditor will

stand to receive Statutory Interest from the date of administration notwithstanding that, absent LBIE's entry into administration, that creditor would not have been entitled to any interest on its claim in respect of the period up until the date of crystallisation. The arbitrariness of this windfall indicates that the interpretation of Rule 2.88(7) which underpins it is misconceived.

44.5 This analysis holds good even in situations where the administration has had the effect of suspending the ability of the creditor or a third party to trigger the contingency. The moratorium which flows from an administration is one which can be lifted in appropriate circumstances and it may be that a contingent creditor would succeed on a request or application to lift the moratorium in circumstances where its operation might prejudice it in the sense of preventing or delaying the falling in of a contingency which would give rise to an actual debt.

44.6 If the debt becomes an actual debt prior to the payment of Statutory Interest, the creditor will be entitled to alter his proof (to the extent necessary) under Rule 2.101 and the administrator will revise upwards his or her estimate of the value of the claim under Rule 2.81. The creditor will, as a result, be entitled: (i) to "catch up" with other creditors in the sense of receiving 100p in the £ on the re-valued proof; and (ii) to receive Statutory Interest from the date on which the contingent debt became an actual debt and, therefore, "outstanding" for the purposes of Rule 2.88(7).

44.7 The process of revaluing a contingent claim, pursuant to the hindsight principle, when the occurrence of the contingency occurs (or becomes more or less likely) is relevant only to the valuing of the proof and no further. See *Stein v Blake* [1996] 1 AC 243, 252, *per* Lord Hoffmann.

See also *Wight and others v Eckhardt Marine GmbH* [2004] 1 AC 147,157 at [32], *per* Lord Hoffman[7].

44.8 In particular, the revaluation process does not "rewrite history" so that the creditor can be said to have been entitled to payment in full as at the date of administration. See *In re MF Global UK Ltd (in special administration)* [2013] EWHC 92 (Ch), at [54][8]. Similarly, the hindsight principle and the revaluation process entailed by it are not of universal application. For example, in relation to the valuation of a client money claim where the CASS rules apply, the notional close-out value of a transaction as at the date of the primary pooling event is not revised in light of any actual subsequent close-out of that transaction. See *In re MF Global UK Ltd (in special administration)* [2013] EWHC 92 (Ch), at [100].

45. In order to assist the Court in relation to this issue, the Administrators will file evidence showing how the Court's adoption of answer (i) or answer (ii) in relation to this issue would impact upon LBIE's administration. In particular, if the Court is minded to adopt answer (i), the Court will be invited to consider what the effect of such a finding would be on the Statutory Interest entitlement of those creditors who have refrained from terminating transactions with LBIE for several years after its entry into administration and thereby may have earned coupon income during that period.

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7 "*These cases on the use of hindsight to value debts which were contingent at the date of the winding up order show that the scene does not freeze at the date of the winding up order. Adjustments are made to give effect to the underlying principle of pari passu distribution between creditors. Hindsight is used because it is not considered fair to a creditor to value a contingent debt at what it might have been worth at the date of the winding up order when one now knows that prescience would have shown it to be worth more. The same must be true of a contingent debt which prescience would have shown to be worth less.*"

8 "*It is relevant to emphasise a feature of the hindsight principle which is of particular significance to the present case. It applies where claims are being estimated. The process of estimation aims to assess the likelihood of the occurrence of the relevant contingency and the amount likely to become due on such occurrence or to predict the outcome of a process of quantifying a sum which is unascertained at the relevant date.*"

Issue 8

46. Issue 8 (relating to future debts) has not been fully argued by the Respondents. All of the Respondents take the position that (i) (the Date of Administration) is the correct answer.

47. It is not clear to the Administrators why Wentworth take the position that (i) is correct, given that its position in relation to issue 7 might lead one to expect that it would take the position that (ii) is the correct answer.

48. In any event, it seems to the Administrators that it is arguable that (ii) is the correct answer. Accordingly, and consistently with the position taken on issue 7 (albeit the Administrators accept that the answer to the two issues is not necessarily the same), the Court is invited to consider the following arguments in favour of (ii) being the correct answer:

    48.1 Like contingent debts, future debts, although provable from the date of administration, become "outstanding" for the purposes of Rule 2.88(7) only when the debt becomes an actual debt.

    48.2 Statutory Interest is payable on future debts only from the date on which the debt becomes due and payable.

    48.3 Until a debt becomes an actual debt, it is not "outstanding" in the sense of being due and payable. It is in that sense that the word "outstanding" is used by the draftsman in Rule 2.88(7). This reflects the fact that, until a debt is due and payable, the administration does not operate so as to keep the creditor out of its money.

    48.4 Further, if Statutory Interest were payable from the date of administration, future creditors would receive a windfall. For example, if a company owed a debt of £100 payable one year after the administration date, why should the creditor, who receives that £100 two years after the administration date, when the administrator pays a first

and final dividend of 100p in the £, be entitled to statutory interest for the period prior to the debt falling due (i.e. the first year of the administration) when no such interest would have been payable outside of the administration and in circumstances in which the creditor was not kept out of his money during that period?

48.5 In addition, in many cases the bargain in which the creditor agreed to accept future payment will itself have already included an element of compensation in respect of the time the creditor has agreed to be kept out of its money (for example interest on a loan).

48.6 Rule 2.105 operates so as to prevent a creditor whose debt is not payable at the date of the declaration of dividend from benefiting from a windfall, by discounting the amount of the creditor's proof (for the purposes of dividend) to reflect the time value of money over the period from the administration date to the date on which the debt is due. It does not operate where the future debt becomes payable prior to the date of the declaration of dividend. It would be perverse if the same draftsman who drafted that rule intended the same creditor to receive Statutory Interest on the entirety of its debt (the discount in Rule 2.105 not applying for the purposes of Statutory Interest) covering that same period.

Issue 6

49. As for issue 6, the positions taken on this issue by Wentworth and the Senior Creditor Group are stated only very briefly. As noted above, this issue arises, in effect, as a potential exception to the answers to issues 7 and 8, in that if the Court considers that, as a general matter, Statutory Interest accrues (in respect of contingent and/or future debts) from the Date of Administration, issue 6 goes to whether, for interest at "*the rate applicable to the debt apart from the administration*", a later date instead applies (i.e. the date on which the debt became due).

50. Wentworth takes the position that (ii) is correct, i.e. that the relevant date is whichever is the later of the date on which the debt became due and the Date of Administration. However, it is unclear to the Administrators whether the Senior Creditor Group takes the position (as it was anticipated to) that (i) (i.e. the Date of Administration) is correct.

51. Accordingly, before the Administrators decide whether or not to take a position on this issue, they invite the Senior Creditor Group to confirm whether or not they do intend to take the position that (i) is correct.

52. In the event that the Court decides that Wentworth's position on issue 6 is correct, then, in order to distribute the surplus effectively, depending on the Court's answer to issues 7 and 8, the Administrators may need further guidance from the Court as to whether, in performing the calculation under Rule 2.88(9), they should make a comparison between (i) the contractual interest that would have accrued from the date on which the debt became due up until the date of discharge and (ii) the sum of Judgments Act Rate interest that would have accrued from the Date of Administration until the date of discharge; or some other comparison (and if so what). In respect of the additional sub-issue identified in this paragraph, the Administrators invite the Respondents in their reply position papers to explain what position (if any) they take.

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

53. It is unclear to the Administrators whether (and if so how) the positions taken by the Senior Creditor Group and Wentworth on this issue differ from one another (noting that York appears to take no position at all). The position papers filed by the Senior Creditor Group and Wentworth are also both very brief on this issue.

54. In the first instance, therefore, the Respondents are invited to clarify in their reply position papers the positions that they take (if any) and to expand upon their reasoning for the positions that they take.

55. Subject to the above, the Administrators make the following preliminary observations (without, at this stage, adopting any formal position):

55.1 A creditor's accession to the CRA might be said not to impact upon the answers to questions 7 and 8 above which questions: (a) raise matters of construction of Rule 2.88 and not of the CRA; and (b) relate to contingent and future debts.

55.2 Clause 25.1 of the CRA provides that a Net Financial Claim (as defined in the CRA) ("**NFC**") shall constitute an ascertained unsecured claim against LBIE (i.e. the claim will neither be contingent nor future).

55.3 It also provides that no interest shall accrue on a NFC, save to the extent provided in Rule 2.88.

55.4 In circumstances in which: (a) the NFC is a new obligation of LBIE's (clause 4.4.2(ii)), which is part of the consideration for the release of the Signatory's Released Claims; and (b) the CRA does not provide for an entitlement to interest save to the extent provided in Rule 2.88, a Signatory is entitled to interest under Rule 2.88(7) on its NFC at the statutory rate (i.e. the rate specified by Rule 2.88(6)) only.

55.5 Clause 19 of the CRA provides that all Open Contracts (as defined in the CRA) between LBIE and a signatory shall be deemed to be terminated. Although this is not one of the specific provisions referred to in question 9, that deemed termination may be an event which caused a future or contingent debt to cease to be a future or contingent debt.

56. Subject to the Respondents' clarification as to the positions they take on this issue, the Administrators have identified a sub-issue, the Court's determination of which would assist the Administrators to distribute the surplus as quickly and efficiently as possible. The sub-issue is whether, subject to the correct answers

to issues 7 and 8, Statutory Interest in respect of a creditor's claim which has been agreed under the CRA is payable from the Date of Administration, from the date of the CRA, or from some other date.

57. In respect of the additional sub-issue identified in the previous paragraph, the Administrators invite the Respondents in their reply position papers to explain what position (if any) they take.

Master Agreements

ISDA

Issues 10 to 18: overview

58. The nine questions arising for determination in relation to issues 10 to 18 relate to the construction and effect of the contractual right to interest under the ISDA Master Agreement.

59. The Administrators consider that the Senior Creditor Group and Wentworth have, between them, adopted all (sensible) available positions in relation to these issues (with York taking no position in relation to any of these issues).

60. There are, however, various reasons why these issues are not yet ready to be set down for a substantive hearing. In particular, the parties would benefit from a further directions hearing to determine whether some of the issues need to proceed to a substantive hearing at all, given that they appear to be agreed between all of the parties, and to set down a procedural timetable for the filing of any necessary expert evidence in relation to certain other issues. The Administrators will, in advance of the Case Management Conference on 21 November 2014, make proposals for the most appropriate approach to any expert evidence.

61. At present therefore, and without prejudice to the possibility that the Administrators may take a different approach in the future, the Administrators take no position in relation to any of these nine issues. However, for the present the Administrators consider that they may provide some assistance to the Court in relation to issues 10 to 18, at least in the following respects:

    61.1 Identifying those issues where there appears to be no dispute between the Respondents, and no (sensible) alternative position, and suggesting how the Court might best dispose of those issues;

61.2 Identifying arguments in relation to those issues which remain "live" between the Respondents where these appear to have been overlooked (for whatever reason) in the Respondents' position papers; and

61.3 Providing evidence as to the context in which the "live" issues arise in LBIE's administration, in order to illustrate the practical effect of the competing arguments advanced by the Senior Creditor Group and Wentworth.

Issues 14, 15 and 18: agreed positions

62. The Senior Creditor Group and Wentworth have effectively reached an agreed position in relation to issues 14, 15 and 18:

62.1 As regards issue 14, there is agreement that a relevant payee's certification of its cost of funding is not conclusive, but that such certification is susceptible to challenge on the basis that it is irrational, in bad faith, or does not relate to a "cost".

62.2 As regards issue 15, there is agreement that it is the Defaulting Party that bears the burden of proving, on the balance of probabilities, that the relevant payee's certification was made irrationally, otherwise than in good faith, or did not relate to a "cost".

62.3 As regards issue 18, there is agreement that the power of a party under Section 7(b) of the 1992 ISDA Master Agreement to transfer any amount payable to it from a Defaulting Party under Section 6(e) without the prior written consent of that party included the power to transfer any contractual right to interest under that agreement.

63. In respect of issue 14, the Administrators consider that the relevant payee's certification is subject to a further requirement, namely that it must be a certification of the payee's cost of funding as properly construed (based, in this

case, in part on the Court's answers to issues 10 to 18 of this Application as applicable), rather than of anything else[9]. The Administrators invite the Respondents to consider this point and set out their position in relation to it in their reply position papers.

64. Subject to the point raised in the previous paragraph, in respect of these three issues, the Administrators do not consider that there is an arguable position other than that on which the Senior Creditor Group and Wentworth agree. Accordingly, the Administrators do not seek to advance a contrary position and intend to invite the Court to give directions in accordance with what has become an agreed position. The Administrators intend to give notice of their intention to do so on the LBIE administration website to give any creditor which disagrees with that approach the opportunity to make an application to intervene if it wishes.

Issues 10 and 13: supplemental arguments

65. At this stage, in relation to issues 10, 11, 12, 13, 16 and 17, the Administrators take no formal position whilst, for the avoidance of doubt, reserving their right to take a formal position in relation to one or more of these issues at a later juncture.

66. However in relation to issues 10 and 13, in the interests of these issues being fully and properly argued, the Administrators bring to the Court's attention what they consider to be arguments supplemental to those set out by the Respondents.

Issue 10

67. Issue 10 concerns whether, on the true construction of the term "Default Rate" as it appears in the ISDA Master Agreement, the "relevant payee" refers to

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[9] See *Lehman Brothers Finance SA (In Liquidation) v Sal Oppenheim jr & Cie KGAA* [2014] EWHC 2627 (Comm), at [53].

LBIE's contractual counterparty or to a third party to whom LBIE's contractual counterparty has transferred (by assignment or otherwise) its rights under the ISDA Master Agreement. Wentworth takes the position that "relevant payee" only refers to the original contractual counterparty. The Senior Creditor Group's position is that the relevant payee is whichever entity is entitled to receive payment of the Early Termination Amount from LBIE, i.e. whether this be the original counterparty or an assignee.

68. In the interests of issue 10 being fully and properly argued, and without taking a formal position, the Administrators draw to the Court's attention a further possible argument that points towards the "relevant payee" being the original counterparty:

68.1 As at the time the parties entered into the ISDA Master Agreement, neither would have known whether it would be the payee in due course.

68.2 In Section 2(e), prior to the occurrence or effective designation of an Early Termination Date, "*if a party defaults in the performance of any payment obligation, [it will]...pay interest on the overdue amount...at the Default Rate*".

68.3 Accordingly, there are circumstances where either "party" could be required to pay interest at the Default Rate.

68.4 Similarly, the definition of "Applicable Rate" contemplates that the Default Rate can be applied to payments made under Section 6(e) by either the Defaulting or Non-Defaulting Party (as defined in the ISDA Master Agreement).

68.5 In the 1992 version of the ISDA Master Agreement, the reference to "relevant payee" in the definition was used to reflect the fact that either party to the agreement could be required to pay the Default Rate (i.e. not just the Defaulting Party), so in turn either could be a payee. It is

accepted that the draftsman could have used the term "relevant party" but the failure to do so does not support the view that the reference to "relevant payee" was intended to capture an assignee.

68.6 Further, if "relevant payee" includes an assignee then there is the potential for abuse where, for example, an existing counterparty effected an assignment to a special purpose vehicle with a very high cost of funding.

Issue 13

69. Issue 13 concerns whether, the "*cost (without proof or evidence of any actual cost) to the relevant payee (as certified by it) if it were to fund or of funding the relevant amount*" should be calculated: (i) by reference to the relevant payee's circumstances on a particular date; or (ii) on a fluctuating basis taking into account any changes in the relevant circumstances (and if so, whether the benefit of hindsight applies when taking into account such changes), in each case, whether or not taking into account relevant market conditions.

70. The Administrators note that neither the Senior Creditor Group nor Wentworth has made reference to the New York Court decision in *Finance One Public Company Limited v Lehman Brothers Special Financing* No. 00 CIV. 6739 (CBM). (S.D.N.Y. Jun. 30, 2003). In that decision, which concerned the "Default Rate" provision in an ISDA Master Agreement governed by the law of the State of New York, the relevant payee had adduced "*ten promissory notes demonstrating the interest rates at which it was forced to borrow funds*", supported by an affidavit. The relevant payee's approach to self-certification, approved by the New York Court, appears to have reflected a calculation of cost of funding on a fluctuating basis taking into account changes in the relevant circumstances, i.e. with reference to the varying rates on which it borrowed funds.

71. The Senior Creditor Group and Wentworth are invited to consider whether (and if so how) this decision of the New York Court impacts their analyses of issue 13.

The context in which "cost of funding" issues arise in the LBIE administration

72. The Administrators consider that it may assist the Court in determining issues 10 to 18 to have evidence before it as to the practical context in which these issues arise in LBIE's administration, and as to the likely practical consequences for LBIE's administration of the competing positions taken on these issues by the Senior Creditor Group and Wentworth. In this regard, the Administrators intend to file evidence which, to the extent necessary, illustrates the various observations made below.

73. First, the Administrators would emphasise the importance, from the point of view of the efficient and expeditious distribution of LBIE's surplus, of receiving clear guidance from the Court as to how they should assess the self-certified cost of funding of ISDA creditors. In particular, as regards issue 14, if the Court decides that a Non-Defaulting Party's self-certification is not conclusive then it will be important for the Administrators to have clarity as to how, in practical terms, they are to approach the scrutinising of ISDA creditors' self-certified cost of funding (including, in light of the Court's directions on the other issues relating to interest arising under the ISDA Master Agreement).

74. As to issue 13, if the Court decides that the cost of funding should be calculated "*on a fluctuating basis taking into account any changes in the relevant circumstances*", then the Administrators will need to be satisfied that the certification given by relevant ISDA creditors has not been calculated irrationally or in bad faith over the whole period during which the debts proved have been "outstanding" (for the purposes of Rule 2.88(7)). It will be time-consuming and expensive for the Administrators to carry out investigations into the propriety of such certificates in circumstances where they are obliged to consider, in respect of each certificate, the way in which

applicable rates have fluctuated over time. Moreover, given that many ISDA creditors will not have had this construction of "*Default Rate*" in mind when self-certifying their cost of funding, it may well be that they will have to re-certify their cost of funding for the relevant period.

75. In respect of issues 11, 12 and 13 in particular, if the Court determines (whether on the basis of expert evidence or otherwise) that an ISDA creditor's cost of funding is related solely to the characteristics of the asset being funded, then this would enable the Administrators to use a single cost of funding as a benchmark for assessing certificates in relation to all ISDA debts in a given currency. To the extent that the cost of funding requires more complex analysis, the Administrators may require more detailed guidance on assessing creditors' claims to interest on such basis.

New York law

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

76. Wentworth takes the positive position that the answers to question 10 to 18 are the same if the underlying Master Agreement is governed by New York law, while the Senior Creditor Group takes the negative position of not contending that the answers would be different if the underlying Master Agreement is governed by New York law. York takes no position in relation to this issue.

77. Despite the apparent agreement between Wentworth and the Senior Creditor Group, given that their positions in relation to most of questions 10 to 18 are distinct, it follows that they in fact take quite distinct positions as to what they contend these answers to be as a matter of New York law.

78. At present, the Administrators take no position in relation to issue 19.

79. The Administrators consider that expert evidence as to New York law will be required to determine issue 19. Wentworth has asserted that it will rely on expert evidence in relation to issue 19 (despite no direction having yet been given by the Court permitting such expert evidence to be relied upon). The Administrators are of the view that the most effective and proportionate way for expert evidence to be adduced in this regard may be for the Court to direct that there should be evidence from a single expert instructed by the Administrators.

80. That approach would ensure that the expert evidence before the Court achieved complete and balanced coverage of all of the issues. The Administrators intend to write to the Respondents setting out their proposals in respect of expert evidence ahead of the Case Management Conference listed for 21 November 2014.

German law

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

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

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

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

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

81. The Administrators consider that the Senior Creditor Group and Wentworth, between them, take all (sensible) available positions on issue 20, although it is noted that the Senior Creditor Group's reasoning is brief on both issues. It is unclear to the Administrators whether Wentworth intends to take a positive position in relation to issue 21. Accordingly, Wentworth is invited to address the issue in its reply position paper.

82. At present, the Administrators take no position in relation to issues 20 and 21.

83. Issues 20 and 21 concern the construction of the German Master Agreement governed by German law, which may require determination with reference to expert evidence on German law. The Administrators are of the view that the most effective and proportionate way for expert evidence to be adduced in this

regard may be for the Court to direct that there should be evidence from a single expert instructed by the Administrators.

84. That approach would ensure that the expert evidence before the Court achieved complete and balanced coverage of all of the issues. The Administrators intend to write to the Respondents setting out their proposals in respect of expert evidence ahead of the Case Management Conference listed for 21 November 2014.

FBF

22. Whether each of:

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

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

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

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

85. Issues 22 to 26 concern the construction of Master Agreements governed by French law, which may require determination with reference to expert evidence on French law. The Administrators are of the view that the most effective and proportionate way for expert evidence to be adduced in this regard may be for the Court to direct that there should be evidence from a single expert instructed by the Administrators.

86. That approach would ensure that the expert evidence before the Court achieved complete and balanced coverage of all of the issues. The Administrators intend to write to the Respondents setting out their proposals in respect of expert evidence ahead of the Case Management Conference listed for 21 November 2014.

87. In relation to issue 22, however, the Senior Creditor Group and Wentworth take the same position on this issue, namely that the various forms of contractual interest set out in the question are all capable of being a "*rate applicable to the debt apart from the administration*" for the purposes of Rule 2.88(9).

88. The Administrators do not consider that there is an arguable position other than that on which the Senior Creditor Group and Wentworth agree.

89. Accordingly, the Administrators do not seek to advance a contrary position and intend to invite the Court to give directions in accordance with what has become an agreed position. The Administrators intend to give notice of their intention to do so on the LBIE administration website to give any creditor which disagrees with that approach the opportunity to make an application to intervene if it wishes.

90. The issue whether any of the various contractual "rates" contemplated in issue 22 are simple or compound has not been included among the issues for determination in the Application. However in its position on issue 22, at paragraph 116, Wentworth argues that French law only permits compound interest if the contract expressly provides for it. By contrast (apparently), the Senior Creditor Group in its position on issue 23, at paragraph 23(1), argues that the interest payable under clause 9.1.1 of the FBF or AFB Master Agreement, where there has been a transfer of rights under these Master Agreements from LBIE's original counterparty to a third party by means of a *cession de contrat*, is calculated on a compound basis.

91. Accordingly, the Senior Creditor Group and Wentworth are invited to clarify in their reply position papers their positions in relation to these questions of simple and compound interest (and give their responses, if any, to the other side's arguments), so that it is clear whether there is any dispute on the point and, in turn so that it may be determined whether the Administrators should apply to amend the list of issues before the Court so to include an appropriately worded additional issue.

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

92. The Administrators consider that the Senior Creditor Group and Wentworth, between them, have taken all (sensible) available positions.

93. At present, therefore, the Administrators take no formal position on this issue.

24. ***Whether the terms:***

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

(ii) "average overnight rates that would be offered to the beneficiary" as it appears in the AFTB Master Agreement;

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

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

94. The Administrators consider that the Senior Creditor Group and Wentworth, between them, have taken all (sensible) available positions.

95. At present, therefore, the Administrators take no formal position on this issue.

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

96. In relation to issue 25, the Senior Creditor Group and Wentworth take the same position on this issue, namely that either the "*party*" pursuant to question 23 or another party authorised to act on behalf of the "*party*" can provide determination and notification of its cost of funding.

97. The Administrators do not consider that there is an arguable position other than that on which the Senior Creditor Group and Wentworth agree.

98. Accordingly, the Administrators do not seek to advance a contrary position and intend to invite the Court to give directions in accordance with what has become an agreed position. The Administrators intend to give notice of their intention to do so on the LBIE administration website to give any creditor

which disagrees with that approach the opportunity to make an application to intervene if it wishes.

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

99. Again, in relation to issue 26, the Senior Creditor Group and Wentworth appear to take the same position on this issue as to the standard applicable in the relevant circumstances, and the Administrators do not consider that there is an alternative arguable position.

100. Subject, therefore, to the Respondents highlighting any material points of difference between them on this issue in their reply position papers, the Administrators intend to invite the Court to give directions in accordance with what has become an agreed position. Again, the Administrators intend to give notice of their intention to do so on the LBIE administration website to give any creditor which disagrees with that approach the opportunity to make an application to intervene if it wishes.

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

(i) ***a Credit Institution or Financial Institution;***

(ii) ***a Fund Entity; or***

(iii) ***a corporate or other type of counterparty.***

101. The Administrators take no formal position on this issue at this stage. However, the Administrators consider that it would assist the Court if the Senior Creditor Group were to respond fully in its reply position paper to Wentworth's position on this issue so that it becomes clear whether there is any dispute in relation to it.

Currency Conversion Claims

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

102. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions in relation to this issue. However this is an issue on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law.

103. Accordingly, the Administrators' position in relation to this issue is that the calculation of a Currency Conversion Claim should not be adjusted to take into account the Statutory Interest paid to the relevant creditor by the Joint Administrators.

104. The Administrators note the Senior Creditor Group's briefly stated arguments in support of this position, but seek to argue this position in their own way.

105. Before answering the question, it is important to understand the nature of a Currency Conversion Claim.

106. A Currency Conversion Claim is premised on the contractual right of a creditor to be paid a debt in a currency (or currencies) other than sterling. Such a claim exists wherever the amount paid to the creditor, in sterling, on its proof, although equal to 100% of the creditor's proof, is, when converted into the relevant contractual currency (or currencies) upon the date (or dates) it is paid, less than 100% of the full amount of the debt expressed in that contractual currency (or currencies).

107. The basis of the claim is as follows:

107.1. First, prior to the insolvency, the creditor was entitled to be paid in a foreign currency. This carried with it the entitlement, if the debt were enforced by action, to obtain a judgment expressed in the foreign currency and to execute against assets in England in a sum of sterling representing the judgment debt converted into sterling at the prevailing exchange rate on the date of execution. See *Miliangos v George Frank (Textiles) Ltd* [1976] AC 443.

107.2. Accordingly, any payment in sterling which, at the relevant exchange rate on the date it was paid, amounted to less than 100% of the amount of the debt expressed in that other currency, would leave a shortfall still owing to the creditor.

107.3. The underlying principle is that, where there is a surplus, the foreign currency debtor should not be entitled to impose on the foreign currency creditor the risk of a fall in value of sterling. See *Re Lines Bros Ltd* [1983] Ch 1, per Brightman LJ at 16D.

107.4. Secondly, the conversion of a foreign currency debt into sterling is solely for the purposes of proving: in an administration, IR 2.86(1) states that a foreign currency debt is to be converted into sterling "*for the purpose of proving...*" and the same expression appears in the context of liquidation in IR 4.91(1).

107.5. The function of the proof process is to arrive at a value for each creditor's debt so as to ensure that distribution of the insolvent estate is on a *pari passu* basis. The requirement to convert all claims into sterling as at the same date is fundamental to the *pari passu* principle.

107.6. Thirdly, the process by which creditors prove their debts, and receive dividends in respect of their proofs, does not operate to discharge, vary or release the underlying contractual right of the creditor, save to the extent that payment in full in respect of the proof in fact exhausts the underlying contractual entitlement of the creditor See *Wight v Eckhardt*

Marine GmbH [2004] 1 AC 147, per Lord Hoffmann at [26]-[27] (*"The winding up leaves the debts of the creditors untouched. It only affects the way in which they can be enforced"*); *Re Lines Bros Ltd* (above), per Brightman LJ at 21F.

107.7. In other words, LBIE's contractual obligation to pay a foreign currency debt in that foreign currency, subsists notwithstanding LBIE's administration, and notwithstanding the requirement to convert that debt for the purposes of proof and distribution of the estate among creditors. It is just that the foreign currency creditor is precluded from taking any action to enforce or recover its foreign currency debt in competition with other creditors, i.e. until all proved debts and statutory interest on such debts have been paid in full.

107.8. Fourthly, if and when LBIE has paid in full all amounts proved against it, plus Statutory Interest down to the date of payment, the restriction on recovery by the foreign currency creditor of the full amount of its foreign currency debt falls away. LBIE is thereafter obliged to make payment of such amount as will ensure satisfaction of the full amount of foreign currency debts, before any surplus is returned to its members.

107.9. This conclusion follows from the fact that the rationale for preventing a foreign currency creditor from recovering in respect of any such shortfall ceases to apply once all proved debts have been satisfied in full. That rationale (as noted above) is that it is the company itself, and not its other (sterling) creditors who should bear the risk of a fall in the value of sterling. Once the interests of other creditors are removed from the equation, the principle underlying the *Miliangos* decision comes back into play: as between the foreign currency creditor and the company (and its members) it is the company (and its members) who should bear the risk of a fall in value of sterling.

108. In the law of contract, there is an important distinction between a claim for payment of a debt and a claim for damages for breach of contract[10]. A debt is a definite sum of money fixed by the agreement of the parties as payable by one party in return for the performance of a specified obligation by the other party or upon the occurrence of some specified event or condition. Damages may be claimed from a party who has broken his contractual obligation in some way other than failure to pay such a debt. It is also possible that, in addition to a claim for a debt, there may be a claim for damages in respect of consequential loss caused by the failure to pay such a debt at the due date.

109. The relevance of this distinction is that rules on the quantification of damages do not apply to a claim for a debt. In particular, the claimant who claims payment of a debt need not prove anything more than his performance or the occurrence of the event or condition on which the sum becomes payable; there is no need for him to prove any actual loss suffered by him as a result of the defendant's failure to pay, neither is there any obligation to mitigate his loss.

110. The majority of LBIE's creditors have debt claims, for example, close-out amounts due under ISDAs, GMRAs and the like. Some, however, have what may be characterised as damages claims for breach of contract (e.g. a failure to deliver or redeliver securities).

111. Where a currency conversion claimant (whose claim is a debt) has received dividends of 100p in the £ which, when converted into the contractual currency, amount to less than the contract debt due to him, he has a residual contractual claim, enforceable as against LBIE once Statutory Interest has been paid in full, for the balance without the need to prove loss.

112. Further, he also has a (prior ranking) claim to Statutory Interest. That claim is a distinct claim which flows from Rule 2.88(7)).

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[10] As to which see *Chitty on Contracts* at §26-008.

113. It follows that, when Statutory Interest is paid to the creditor, the payment goes to discharge LBIE's liability to pay Statutory Interest. There is no question of appropriation. Notwithstanding that there are two debts owed to the creditor (Statutory Interest and the Currency Conversion Claim), the payment of Statutory Interest must go to discharge the prior ranking debt, i.e. Statutory Interest.

114. Whilst Statutory Interest might be characterised as a "*benefit... received under the insolvency regime*" (see the *Waterfall* judgment at [99]), it is a benefit received by all creditors and it amounts to statutory compensation for them having been kept out of their money during the administration process. Payment of Statutory Interest (whether at or above any contractual rate) is also an obligation of the company in administration.

115. Accordingly, payment of Statutory Interest does not reduce the amount of a Currency Conversion Claim based on the receipt, by way of dividends, of less than the claimant's contract debt. Such payments simply discharge a separate and distinct statutory debt.

116. The currency conversion claimant suing in debt is not required to prove any loss. He is merely required to prove that his contract debt was more than the amount paid to him by way of dividends, when converted back into the contractual currency or currencies at the date or dates of distribution; the Currency Conversion Claim is simply the undischarged portion of the sum owed. If this is correct, the benefit he receives by way of Statutory Interest[11] is irrelevant to his claim. It cannot be taken to have reduced the amount for which he is otherwise entitled to claim.

117. If and to the extent that the currency conversion claimant were required to treat payment of Statutory Interest as reducing his Currency Conversion Claim, the result would be that he would, in effect, receive less Statutory

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[11] Which is, in any event, no real benefit to the extent that he has a contractual right to interest at a rate of in excess of 8%.

Interest than those creditors who had no currency conversion claim (because the dividends they had received were sufficient to discharge their contractual debt). There is no justification for that result.

118. As noted above, some of LBIE's creditors may have damages claims against LBIE, for example, for client assets not returned to them or returned late. Additionally, as referred to above, it is possible that, in addition to a claim for a debt, there may be a claim for damages in respect of consequential loss caused by the failure to pay such a debt at the due date[12].

119. Where a currency conversion claimant's provable debt is a claim in damages which are payable in a foreign currency, the position is more difficult because it is required to prove actual loss.

119.1. In that situation, where the creditor has received dividends of 100p in the £ together with Statutory Interest, in asserting his currency conversion claim he will be required to prove actual loss.

119.2. In that regard, assuming that he had no right to interest other than under Rule 2.88(7) (or a right to receive interest at a lower rate), it might be said that the receipt of Statutory Interest (or the sum in excess of any pre-existing right) has to be taken into account in quantifying the claimant's actual loss because:

(a) The loss is caused by the intervention of the statutory scheme which will also have caused a benefit in the form of an entitlement to Statutory Interest. This will not always be the case, however. The damages claim might have arisen prior to the commencement of the administration and, in any event, the loss is caused not by the intervention of the statutory scheme but by the failure to deliver securities or other breach of contract or duty by LBIE; or

[12] It is only if the damages claim is in a foreign currency that a Currency Conversion Claim will arise, such that the issue under discussion arises at all.

(b) The creditor should, in quantifying its loss, give credit for what it has received from LBIE including the Statutory Interest paid.

120. The Administrators submit that any such argument would be wrong. The claimant had a freestanding statutory right to Statutory Interest (alongside, and *pari passu* with, other creditors, e.g. those with damages claims arising in sterling) and the payment of it merely discharges LBIE's obligation to pay Statutory Interest and is not relevant to the question of loss.

29. Whether there exists a non-provable claim against LBIE where the total amount of interest received by a creditor applying the Judgments Act Rate on a sterling admitted claim, when converted into the relevant foreign currency on the date of payment, is less than the amount of interest which would accrue applying the Judgments Act Rate to the original foreign currency claim.

121. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions in relation to this issue. However, this is an issue on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law.

122. Accordingly, the Administrators' position is that no Currency Conversion Claim exists in the relevant circumstances.

123. The Administrators note Wentworth's briefly stated arguments in support of this position, but seek to argue this position in their own way.

124. Under Rule 2.88(7) interest is payable on "debts proved" and, under the Rules, debts are converted into sterling in order to be proved. The statutory rate of 8% per annum is therefore applicable to the amount of the sterling debt proven.

125. The basic principle on which the Currency Conversion Claim is based is that a creditor who has a contractual right to be paid in a foreign currency and has been prejudiced by the application of the statutory scheme which requires it to

be paid in sterling, should, in the event of a surplus, be able to bring a non-provable claim in respect of the undischarged part of its debt that remains as a result.

126. The above principle does not apply in the context of the question posed. The creditor would never have been entitled to receive interest at a rate of 8% on its original Currency Conversion Claim (unless specified in the relevant contract). Rather, the claim to Statutory Interest is itself an entitlement arising by virtue of the statutory scheme and accrues on the proved claim, which is a sterling amount.

127. Accordingly, a creditor would be unable to assert that its rights had been prejudiced, and it had suffered loss, as a result of the 8% Statutory Interest being payable only on a sterling amount, since the right to Statutory Interest at 8% arises only as a result of the statutory scheme itself.

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

128. The Respondents appear to take the same position on this issue, namely that a non-provable claim does exist in the relevant circumstances. This is an issue in respect of which the Administrators do not consider that there is an arguable position other than that on which the Respondents all agree.

129. The Administrators have identified a potential variation on this issue. It is possible that the total amount of interest received by a creditor on a sterling admitted claim, when converted into the relevant foreign currency on the date (or dates) of payment, will be less than the amount of interest which would have accrued applying the "rate applicable to the debt apart from the administration" to the original foreign currency claim, whether the interest in

fact received was at a "rate applicable to the debt apart from the administration" or at the Judgments Act Rate[13]. The Administrators invite the Respondents to consider this point and set out their position in relation to it in their reply position papers.

130. Subject to the point raised in the previous paragraph and the Respondents' positions on it, the Administrators do not seek to advance a contrary position and (if the position is agreed) intend to invite the Court to give directions in accordance with what has become an agreed position. The Administrators intend to give notice of their intention to do so on the LBIE administration website to give any creditor which disagrees with that approach the opportunity to make an application to intervene if it wishes.

31. ***Whether:***

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

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

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

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[13] I.e., even where the Judgments Act Rate applies because it is higher than any contractual rate (albeit only where the difference is fairly small), the relevant currency movement might still cause the creditor to receive less interest than it would contractually have been entitled to in the foreign currency.

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

131. These two issues are highly fact-specific. Wentworth, at paragraph 144 of its position paper, refers specifically to a particular kind of GMSLA, a PB and an MLA (as defined by Wentworth) and answers issues 31 and 32 in the negative with reference to these agreements. By contrast, the Senior Creditor Group contends that a Currency Conversion Claim can arise in certain circumstances, but without advancing any arguments in support of this contention, and without reference to any particular master agreements.

132. At present, the Administrators do not take a positive position on either issue 31 or issue 32.

133. The Administrators' view is that, in light of the high fact-specificity of these two issues and the distinct ways in which the Respondents have approached them, it would assist the Court if the Respondents could agree on which particular master agreements they consider these two issues go to[14].

134. The Administrators reserve the right to take a position on one or both of issues 31 and 32 once it has been agreed between the parties which particular master agreements arise for consideration.

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

(i) the provable debt;

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

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

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[14] See the reference to "other master agreements" in Issue 31(iii).

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

135. In their position papers the Senior Creditor Group and Wentworth have put their positions on issue 33 very briefly, with the former stating its position to be subject to (inter alia) receipt of Wentworth's position paper.

136. At present, the Administrators do not take a positive position on issue 33.

137. However, in light of the way that the Respondents have approached this issue in their position papers, the Administrators invite the Respondents to file evidence of transfer agreements with the features outlined in the question (LBIE and the Administrators not being party to such agreements) so that the parties can consider and set out their positions (in supplemental position papers as required) and, in turn, the Court may give a direction which best assists the Administrators in distributing the surplus.

Effect of Post-Administration Contracts

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

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

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

(iii) the CRA.

138. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions on this issue and have presented their positions fully. It is anticipated that this issue will be further developed by the Respondents when they file their reply position papers (having seen how each other puts its case). It is also apparent that the Respondents may wish further to develop their arguments in evidence. The Senior Creditor Group in particular makes reference to a factual matrix that has not been developed by them in evidence. In the circumstances, the Administrators at present do not take a formal position but reserve the right to comment upon this issue at a later stage in light of further evidence filed and (as required) directions from the Court.

139. Accordingly, for present purposes the Administrators limit themselves to making the following comments in response to the Respondents' position papers:

139.1 The Administrators note that York's position on the extent of the release clause, at paragraph 73 of its position paper, appears to ignore the words "*whether in existence now or coming into existence at some point in the future and whether or not in the contemplation of the Creditor and/or* [LBIE] *and/or the Administrators at the date hereof*", as contained in the Foreign Currency CDDs. York is invited to consider whether these might not be precisely the kinds of words that

constitute "*express and specific language*" and, if so, how this affects its position.

139.2 As to paragraph 152 of Wentworth's position paper, the Administrators consider that they have put before the Court examples of all the CDD wording the Court is being asked to construe (without putting into evidence every possible variation of every template). The Administrators have not suggested, nor do they suggest, that the CDDs exhibited to the tenth witness statement of Anthony Victor Lomas dated 25 July 2014 ("**Lomas 10**") constituted a representative sample of CDDs entered into by creditors. Instead, the Administrators have provided an example of each template (which, being the most recent version, will generally include both the Statutory Interest and Currency Conversion Claim carve-out language). Furthermore, the Administrators have also provided, at pages 494 to 526 of the exhibit to the ninth witness statement of Anthony Victor Lomas dated 11 June 2014 ("**Lomas 9**") a copy of a CDD that pre-dated the inclusion of any carve-outs to deal with Statutory Interest or Currency Conversion Claims. The development of the CDDs, including the addition of the carve-outs to deal with Statutory Interest or Currency Conversion Claims, at the relevant times, is explained in Lomas 10.

139.3 The Court will be asked to consider such variations to the relevant provisions contained in the CDDs as (a) are necessary to provide the Administrators with useful guidance and (b) it is argued by the parties to the Application could require separate consideration as a result of a material difference existing. The Administrators consider that the parties are able, from the material exhibited to both Lomas 9 and Lomas 10, to identify any provisions, or different templates, that they say could lead to a different construction. The differences might most usefully be presented at trial in, for instance, tabular form that identifies each template where the parties consider a different construction might arise and, in respect of each such template, those variations (e.g. inclusive or otherwise of the Statutory Interest and/or

Currency Conversion Claim carve-outs) that in turn lead to a potentially different construction.

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

(i) ***a CDD incorporating a Release Clause; or***

(ii) ***the CRA.***

140. The Administrators consider that the Respondents have, between them, taken all (sensible) available positions in relation to this issue and have argued their positions fully.

141. The issue concerning Statutory Interest is of importance to all unsecured creditors and, as appears from the Respondents' position papers, is unlikely to be the subject of significant (if any) further evidence. Consequently, the Administrators consider that it is in the interests of the unsubordinated unsecured creditors for them to set out their position.

142. On this issue the Administrators take the position that a creditor's claim to Statutory Interest has not been released in the relevant circumstances.

143. Turning first to the CDD, and adopting the defined terms which appear therein:

143.1. The CDD is concerned with the quantification of a creditor's claim and not with distribution. This is clear from the recitals to the CDD.

143.2. The CDD constitutes an agreement as to the quantum of the Agreed Claim, that quantum being the Agreed Claim Amount.

143.3. One of the purposes behind agreeing the quantum of the creditor's claim is that, after the deduction of any part of the Agreed Claim which represents the proprietary element of a client money claim through the

mechanism in clause 3 of the CDD, the Agreed Claim will become an Admitted Claim.

143.4. An Admitted Claim is a claim which "*qualifies for dividends from the estate of the Company available to its unsecured creditors pursuant to the Insolvency Rules and the Insolvency Act*".

143.5. Given that the agreement of an Agreed Claim is reached in anticipation of it becoming an Admitted Claim (in whole or in part), it is capable of including provable interest but not Statutory Interest. Statutory Interest is payable on provable claims rather than constituting part of a provable claim.

144. The release provision at clause 2.1.2 does not apply to the Agreed Claim. The Agreed Claim is carved out from what is released ("*[s]ave solely for the Agreed Claim*").

145. The right to receive Statutory Interest is a right which is consequential and parasitic on the creditor having an Admitted Claim, in the same way as the right to receive dividends. It forms part of the bundle of rights arising on the coming into existence of the Admitted Claim. Therefore it is preserved by the proviso. If the Agreed Claim is not released, the right to receive Statutory Interest out of any surplus available after the payment in full of the debts proved is similarly not released because it is not a freestanding right. It is part and parcel of the claim which qualifies for dividends.

146. If and to the extent that the wording is considered by the Court to be ambiguous, which the Administrators do not consider it is, then the Court is required to adopt the more commercially sensible reading of the clause, consistent with the guidance of the Supreme Court in *Rainy Sky v Kookmin Bank* [2011] 1 WLR 2900. The more commercially sensible construction of clause 2 leads to the same conclusion as was reached above. This is because the purpose of the CDD was to establish the quantum of creditors' agreed claims, with a view to them becoming established claims, and it would have

made no commercial sense for creditors to have abandoned a contingent right to Statutory Interest merely in order to have certainty as to the amount for which they would be admitted to proof and there is no obvious reason why the Administrators, acting consistently with their statutory duties, would have seen fit to require creditors to abandon such right.

147. As for the CRA, where a claim has been compromised pursuant to the CRA, the provable debt of the creditor is the NFC which will, under the Rules, and as acknowledged in the CRA at clause 25.1, accrue interest in accordance with Rule 2.88. The signatory's debt under a Financial Contract (as defined in the CRA), to which a contractual rate may have been applicable, is released and replaced with the NFC. Since there is no "rate applicable" to the NFC apart from the administration, the Administrators consider that such claim accrues interest under Rule 2.88(9) at the Judgments Act Rate.

148. Finally, the Administrators make the following observations in relation to the Respondents' position papers on this issue:

148.1 The Administrators note that Wentworth contends, at paragraph 163 of its position paper, that the CDDs operate so as to release the creditor's contractual entitlement to interest, such that Statutory Interest is payable to it at the Judgments Act Rate, but it does not contend that the CDDs operate so as to release Statutory Interest at the Judgments Act Rate. The Administrators consider it to be at least arguable (although it is contrary to their own position) that the CDDs operate so as to release Statutory Interest at the Judgments Act Rate in these circumstances. Therefore Wentworth is invited to consider running this argument in its reply position paper in order to assist the Court.

148.2 As to the Senior Creditor Group's alternative position that the CRA and CDDs should be subject to rectification, the Administrators question whether the Court is able to address this highly fact-specific question in this Application, given that (inter alia) (i) no claim for rectification is before the Court and (ii) it is not practicable, in an

application such as the present, for the parties to file the appropriate (and sufficient) evidence so as to enable the Court to determine the rectification issue.

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

149. At present, the Administrators do not take a positive position on this issue. The Respondents' position papers do not set out in any detail their positions (and it is noted that Wentworth intends to respond to the Senior Creditor Group's position in its reply position paper).

150. The Administrators consider that this issue is a highly fact-specific one which may not, therefore, be suitable for determination by way of the present Application. Furthermore, issue 36 only arises if the Court determines in relation to issues 34 and/or 35 that there has been a relevant release. The Respondents' position papers allude to (without expressly raising or setting out in accompanying evidence) factual matters said to be relevant to the issue. Accordingly, the Administrators reserve their right to respond in light of the Respondents' positions (once fully articulated) and any evidence is filed.

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

151. In relation to this issue, Wentworth has taken the position that, where it is not possible to ascertain how the agreed claim in a CDD is derived from the underlying claims, the claims are to be calculated on a pro rata basis by reference to the underlying claims.

152. However the Senior Creditor Group has not addressed whether or not, in circumstances where it is unclear how a single agreed claim in a CDD derives from its component underlying claim, the Administrators should approach an

agreed claim in a CDD by simply prorating the applicable rates across the component underlying claims. Accordingly, the Senior Creditor Group is invited to clarify in its reply position paper whether (and if so on what basis) it takes an adverse position to Wentworth on this point.

153. At present, the Administrators do not take a positive position on this issue.

154. For the avoidance of doubt, issue 37 is a matter of significant practical importance for the Administrators, given that the issue has in fact arisen in a significant number of cases.

155. Briefly for present purposes, the issue arises where a creditor and LBIE entered into a CDD and:

155.1 the CDD compromised a number of component underlying claims (as set out in the creditor's proof of debt);

155.2 the amount of the claim admitted by the CDD was lower than the total value of the component underlying claims asserted by the creditor[15]; and

155.3 the CDD did not record (and the parties did not reach any other binding, express agreement as to) the extent to which and how the agreed claim set out in the CDD derived from the component underlying claims.

156. In this situation, the Administrators require guidance as to the value to be attributed to the component underlying claims where this impacts upon the creditor's entitlements in respect of Statutory Interest and/or Currency Conversion Claims, including as to:

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15 Although the issue might potentially arise even when admitting a creditor's claim in full where there was no agreement as to the constituent parts, with LBIE's view of one part of the debt being higher than the creditor's view, while being lower than the creditor's view of another part.

156.1 whether the Administrators are entitled and/or required to pro-rate the amount of the agreed claim across the component underlying claims, and if so on what basis (for example on the basis of the proof of debt, the Administrators' view of the value of the component underlying claims, or some other basis);

156.2 whether the Administrators are entitled and/or required to engage in any more detailed assessment as to the value properly to be attributed to the component underlying claims, and if so how they ought to do so (for example, by reference to what sources of information); and

156.3 how any disputes as to the value properly to be attributed to the component underlying claims are to be dealt with.

157. The Administrators intend to file further evidence in order to illustrate the contexts in which the issue has arisen so as to assist the Court in determining the issue.

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

158. The Administrators consider that the Senior Creditor Group and Wentworth have, between them, taken all (sensible) available positions in relation to this issue. However, this is an issue on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law.

159. Accordingly, the Administrators' position is as follows:

159.1 In 2009, the CRA was entered into by LBIE and a number of counterparties to resolve issues surrounding their entitlements to trust assets held by LBIE and under which "Signatories" gave up their

existing claims in return for new claims to trust property and unsecured claims against LBIE.

159.2 Amongst other things, under the terms of the CRA, all of the counterparty's claims under "Financial Contracts" were exchanged for an unsecured NFC.

159.3 The CRA provides, at clause 4.4.4:

> *"All Signatories shall have their Released Claims exchanged for the following, as appropriate:*
>
> *(i) the right to have their Net Contractual Position, Allocations, Distributions and Appropriations determined on the basis set out in this Agreement;*
>
> *(ii) the right to claim as a new obligation of the Company their Net Financial Claim (if any)...."*

159.4 Clause 25.1 of the CRA provides that:

> *"A Net Contractual Position in respect of a Signatory expressed as a positive number will represent an amount due and owing by the Company to that Signatory, which shall constitute an ascertained, unsecured claim of that Signatory in the winding-up of the Company or any distribution of the Company's assets to its unsecured creditors (such Claim, a "**Net Financial Claim**"). 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."*

159.5 Under the CRA the Net Contractual Position is arrived at by aggregating all Close-Out Amounts (broadly, amounts payable under Financial Contracts upon termination). Close-Out Amounts not already denominated in US dollars are converted in to US dollars using the Spot Rate at the close of business in London on 15 September 2008. Whilst the aggregate of the close-out amounts under the Financial Contracts are used in calculating the Net Contractual Position which underpins the NFC, the relevance of the Financial Contracts is for valuation of the NFC only. Any right to payment of the Close-Out

Amounts pursuant to the Financial Contracts is released, in exchange for the NFC.

159.6 The NFC is a new claim which exists only for the purposes of receiving a dividend from the insolvent estate. The NFC is defined as an unsecured claim of the Signatory in the winding up or any distribution of LBIE's assets and such claim constitutes a provable claim only. The words "*which shall constitute an ascertained, unsecured claim of that Signatory in the winding-up of the Company or any distribution of the Company's assets to its unsecured creditors*" are unambiguous in their meaning.

159.7 Accordingly, the Administrators' position is that Part VII of the CRA is not capable of giving rise to a Currency Conversion Claim.

Compensation for Time Taken to Discharge Non-Provable Claims

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

160. The Administrators consider that the Respondents, between them, have taken all (sensible) available positions in relation to this issue. However, this is an issue on which the Administrators, as experienced insolvency practitioners, consider that they should adopt a positive position, being a matter of insolvency law.

161. Accordingly, the Administrators' position in relation to this issue is that a creditor is entitled to no form of compensation in the relevant circumstances.

162. Rule 2.88(7) provides that "*any surplus remaining after payment of the debts proved shall, before being applied for any purpose, be applied in paying interest on those debts in respect of the periods during which they have been outstanding since the company entered administration*".

163. In circumstances where a creditor's provable debt has been paid in full but the Statutory Interest which had accrued on this principal debt prior to that payment is not itself paid until some time later, there can be no scope for further Statutory Interest to accrue under Rule 2.88(7) on the amount of Statutory Interest which remains payable and outstanding after the payment of the principal debt.

164. This is because Rule 2.88(7) provides for Statutory Interest to accrue only "*on those debts*", i.e. "*the debts proved*". On the proper interpretation of Rule 2.88(7), Statutory Interest does not accrue on any debts other than the debts proved. Therefore, Statutory Interest cannot accrue (for or in respect of the

time taken for such claims to be discharged) either on a Statutory Interest claim or on any other non-provable claim, since neither type of claim can be characterised as being among "*the debts proved*".

165. Further, insofar as a Statutory Interest claim is concerned, there is no obvious alternative basis on which it could accrue interest.

166. Section 17 of the Judgments Act 1838 provides that: "*Every judgment debt shall carry interest at the rate of 8 pounds per centum per annum from such time as shall be prescribed by rules of court... until the same shall be satisfied...*" A Statutory Interest claim cannot be characterised as a "*judgment debt*" in the relevant sense.

167. Further, Rules 2.88(3) and (4) provide for interest to accrue on a "*debt*" at the rate which is specified in section 17 of the Judgments Act 1838 (see Rule 2.88(6)). They apply only to interest accruing up to the company's entry into administration and, in any event, the word "*debt*" is defined in Rule 13.12(1) so as to extend only to provable debts (including provable interest but not including Statutory Interest). Further, Rules 2.88(3) and (4) are themselves framed in terms which make it clear that they do not contemplate the accrual of interest on a Statutory Interest claim.

168. Furthermore, creditors are unable to frame a claim against LBIE for damages for loss or in restitution on the basis that they have been kept out of their money in respect of an unpaid Statutory Interest claim. Rule 2.88(7) does not itself stipulate a precise time at which Statutory Interest will become payable, instead framing the timing of the administrators' obligation to pay Statutory Interest simply in terms of being "*before* [the surplus is] *applied for any purpose*". Accordingly, a Statutory Interest claimant will be unable to demonstrate that it has in fact been kept "out of its money" (or that LBIE had incurred any unjust enrichment as a result of Statutory Interest being paid at a particular time). If an administrator was, for no good reason, failing to distribute the surplus to those entitled to receive Statutory Interest (which is not the case in this instance – the Administrators cannot distribute the surplus

at present because of the uncertainty created by: (i) the Waterfall appeal; and (ii) the issues raised in this application), doubtless an application could be made to the Court for directions requiring its office holder to distribute. However, there would be no basis on which the creditor could claim compensation in respect of the delay, whether the delay was justified or not.

169. As to non-provable claims, again Statutory Interest cannot accrue on such a claim under Rule 2.88(7), since such claims are not among "*the debts proved*" for the purposes of the wording of that provision.

170. Again, interest cannot accrue on such claims at the Judgments Act Rate, whether directly by way of section 17 of the Judgments Act 1838 or indirectly by way of Rule 2.88(3) or (4), for the same reasons as set out above in relation to Statutory Interest claims.

171. Finally, a creditor has no claim against LBIE for damages for loss or in restitution against LBIE on the basis that it has been kept out of its money in respect of an unpaid non-provable claim. A non-provable claim only falls to be paid after Statutory Interest has been paid. As noted above, Rule 2.88(7) does not itself stipulate a precise time at which Statutory Interest will become payable, instead framing the timing of the administrator's obligation to pay Statutory Interest simply in terms of being "*before* [the surplus is] *applied for any purpose*".

William Trower QC
Daniel Bayfield
Alexander Riddiford
Linklaters LLP

10 October 2014